CHAPTER 7

THE 70TH ANNIVERSARY OF THE COUNCIL OF ECONOMIC ADVISERS

Almost exactly 70 years ago, on February 20, 1946, President Harry Truman signed the Employment Act of 1946 into law. Born out of America's experience during the Great Depression, this law reflected Congress's desire to prevent an economic calamity of that scale from ever recurring. Yet the immediate practical consequences of the Employment Act were modest: it created two institutions, the Joint Economic Committee on the Economic Report—subsequently renamed the Joint Economic Committee (JEC)—and the Council of Economic Advisers (CEA). Together with the JEC, it was hoped that CEA would help to "defend the ramparts against depression" (Flash 1965).

CEA is in many ways a distinctive institution, both within the administration and in the international context. The CEA chair reports directly to the President on economic issues, but CEA has no regulatory authority and few prescribed operational responsibilities. For most of its history, CEA has had a small staff drawn mostly from the academic economics community and hired on the basis of professional expertise. The views it expresses are grounded in economic analysis, and are based on applying economic theory and empirical research to the often-novel situations in which policymakers find themselves.

However, CEA is also a part of the Executive Office of the President, working collaboratively with other departments within the Executive Office of the President and the administration more broadly to advance the President's agenda. CEA plays a distinctive role in the administration, but like other components of the administration, it also communicates and operates as part of a team on behalf of the President.

While the Council has made useful contributions to economic policy-making throughout its history, its role and influence have varied depending on the needs of the President, the economic issues facing the country, and the personnel of CEA itself. Because CEA has no fixed statutory responsibilities except for assisting in the preparation of the annual *Economic Report of the President,* its role and influence depend on the degree to which it can be useful and relevant to the President and other senior decision makers.

On the 70th Anniversary of the Employment Act of 1946, this chapter explores the origins of the Council of Economic Advisers, describes its core functions, and examines several key moments from its history. The chapter first examines the legislative origins of CEA and provides an overview of its institutional structure and policy priorities. It then focuses on four interrelated functions of CEA: helping to develop and evaluate economic policies for consideration by the President and the administration; helping to advance the President's economic agenda; gathering, analyzing, and interpreting information on economic trends and developments, and informing the President about the state of the economy; and engaging the economics community. The chapter draws on historical examples and former CEA chairs' and members' accounts—including boxes from six former chairs about their experiences at CEA—to illustrate each of these functions and their inherent challenges, and identifies several institutional lessons for ensuring CEA's continued effectiveness.

Goals and Duties

Origins of CEA—Legislative History of the Employment Act of 1946

The Employment Act ultimately signed into law in February 1946 was markedly different from the original bill that Senator James E. Murray introduced in the Senate in January 1945. The original Senate bill (S.380), which was called the Full Employment Act, aimed to "set postwar economic policy in a simple Keynesian mold" (Stein 1988), through "solidly entrench[ing] a strong bias toward active countercyclical fiscal policy in the core of the American executive branch" (DeLong 1996). S.380 provided that the government first define full employment, and then "establish and maintain programs to ensure an inflation-free, fully employed economy" (Mills 1988). The operational plan included the following key points:

> *(1) [I]t would be the responsibility of the federal government to ensure that anyone wishing to work would be able to locate a job; (2) the [P]resident was to prepare each year a National Production and Employment Budget which would include estimates of the size*

and composition of the labor force, investment plans for all levels of government, plus those of the private sector; (3) if insufficient investment existed to provide full employment, then the [P]resident would develop programs to achieve this level of employment. He was to have similar responsibility for, and powers over, the control of inflation; (4) this budget was to be prepared in the Executive Office of the President; and (5) this bill would establish a Joint Congressional Committee on the National Budget to study the [P]resident's document and either recommend or change any legislation implied in it" (Mills 1988).

By contrast, the House substitute bill, called the Employment and Production Act of 1946, "rejected the fundamental principles of the Senate bill" (Bailey 1950). It removed the declaration of the Federal Government's responsibility for maintaining full employment, the accompanying commitment of government resources, the affirmation of the right to employment opportunity, and the National Production and Employment Budget program. It also provided for a Council of Economic Advisers to be "composed of three members at $15,000 a year, whose duties were to submit recommendations to the President whenever inflation or unemployment threatened, to consult with economic groups, and to submit annual and quarterly reports on economic trends" (Bailey 1950).

The Employment Act that emerged from the Joint Conference Committee and was signed into law reflects an attempt to reconcile the profoundly different economic views contained in the House and Senate bills. In the final law, the words "full employment" were ultimately replaced with "maximum employment, production and purchasing power." The law also included language specifying that part of the Federal Government's purpose is "to foster and promote free competitive enterprise." Instead of the National Production and Employment Budget, the law called for an annual *Economic Report of the President*, "setting forth . . . current and foreseeable trends in the levels of employment, production, and purchasing power . . . and a program for carrying out the policy [to promote] conditions under which there will be afforded useful employment for those able, willing, and seeking to work" (Employment Act 1946; DeLong 1996). Meanwhile, the language from the House bill establishing the Council of Economic Advisers was kept mostly intact.[1]

[1] The law also established what is now known as the Joint Economic Committee, a standing joint committee of Congress, whose original functions were to coordinate economic policymaking, to monitor the subjects in the *Economic Report*, and to produce its own yearly report in response to the President's *Economic Report* (Tollestrup 2015).

The balance struck in the final Employment Act meant that CEA's role could be interpreted differently depending on whether one emphasizes the language from the House bill or from the Senate bill. Because of this dichotomy, from the beginning, the Council faced "a divergence of expectations regarding its brand of economic analysis, its policy recommendations, and its mode of operations" (Flash 1965). Consistent with that initial diversity of views, CEA has focused on different policies over the course of its history, as discussed in this chapter.

Institutional Structure

CEA has an unusual—and perhaps unique—institutional structure. Partially due to concerns about Executive Branch overreach during the Roosevelt Administration, Congress intentionally provided CEA with limited resources and specified a Council of three rather than one single adviser. CEA is currently headed by a chair and two members, each of whom is required to be "exceptionally qualified" to analyze economic developments and recommend economic policy (Employment Act 1946).[2] Today, CEA's staff is composed of academic economists and economics graduate students who are on leave from their university positions, career government economists on temporary assignment from other agencies, some recent college graduates who have studied economics, and a small statistical, forecasting, and administrative staff.

Unlike in many other governments, where the top professional economist reports to the finance minister or another cabinet minister, the CEA chair is expected to participate at the Cabinet level in discussions about economic policy. Although in some other countries, such as Germany, the government has a separate set of economic advisers who are expected to make independent recommendations, they are not integrated into day-to-day government decision-making in the same way as CEA.

CEA's institutional structure has shaped the role that it plays in economic policymaking. For example, CEA's lack of regulatory authority and its few operational responsibilities mean that its influence depends largely on its relationship with the President and the rest of the Executive Branch. As such, CEA's influence has waxed and waned at various points in its history, depending on the strength of these relationships as well as the soundness and persuasiveness of its analysis. However, CEA's position in the Executive Office of the President also allows it to take a broader perspective on economic policy and place less weight on the day-to-day exigencies of running the Federal Government. As former CEA Chairman Martin Feldstein put

[2] As a result of the Presidential Appointment Efficiency and Streamlining Act of 2011, the two non-chair CEA members no longer require Senate confirmation.

it, "[t]he CEA and its chairman have the luxury of trying to discern what is in the best interest of the country and of providing that analysis and advice directly to the [P]resident and to the cabinet as a whole" (1992).

Similarly, CEA's small size has also had a strong influence on how it functions. Being a small organization has enabled CEA to be more flexible, efficient, less rigid and hierarchical, and less formal than would be possible otherwise. However, it also means that CEA plays a limited role in more expansive and resource-intensive matters, consistent with its lack of formal regulatory and operational responsibilities.

Both Roger Porter, a scholar of the American Presidency and former White House economic adviser, and former CEA Chairman R. Glenn Hubbard argue that CEA's small size, its professional reputation, and its limited operational responsibilities have contributed to its longevity (Porter 1997; Hubbard 2002). Porter notes that "of the nearly 50 entities that have been located in the Executive Office of the President since it was created in 1939, the CEA is one of only 11 that remain" (1997).

Policy Focus

CEA's policy focus has evolved over the years. While countercyclical fiscal policy was the focus of the Employment Act of 1946, CEA has long since worked on a variety of other microeconomic and macroeconomic issues. For example, CEA works on macroeconomic subjects such as long-term growth, financial markets, and international macroeconomics. CEA helps to frame public discussions on macroeconomic policy, and it chairs the "Troika" forecasting process—an interagency system first formed during the Kennedy Administration, in which the Council of Economic Advisers, the Department of the Treasury, and the Office of Management and Budget jointly produce regular macroeconomic forecasts used for planning the President's Budget (see Box 7-1 for former CEA Chair Laura D'Andrea Tyson's discussion of the difficulty of economic forecasting and the role of fiscal policy in the Clinton Administration).

While macroeconomic issues continue to be an important part of CEA's portfolio, in recent decades CEA has devoted an increasing amount of attention to microeconomic issues that arise in the context of legislation, regulatory processes, and other administrative actions. Former CEA Chairman Charles Schultze reports that the proportion of CEA's annual *Economic Report* focused on microeconomic subjects grew dramatically from 1947 through 1995 (1996).

This evolution is due to a number of factors. In part, it reflects a reduced emphasis by the economics profession on fiscal policy as a macroeconomic tool and an increased recognition of the importance of monetary

Box 7-1: Former CEA Chair Laura D'Andrea Tyson (1993 – 1995)

A primary responsibility of CEA along with OMB and the Treasury is the development of economic forecasts on which the administration's annual and long-term budget projections depend. The budget deficit, widely used as an indicator of fiscal policy stance and central to political debates, is highly sensitive to the economy's performance. Yet forecasting that performance is an exercise fraught with uncertainty and subject to significant errors that get larger as the forecasting period lengthens.

In January 1993, at the beginning of the Clinton Presidency, the economy was underperforming relative to forecasts, and much weaker than expected macroeconomic conditions were producing much higher than expected budget deficits. Confronting a deteriorating budgetary outlook, the new Clinton CEA worked with the rest of the Clinton economic team to develop a budget plan to cut the deficit by $500 billion over 5 years while honoring the President's top fiscal priorities to increase public investment and expand the earned income tax credit. The administration's economic forecasts underpinning this plan reflected the prevailing consensus among economists that the growth rate of potential output was around 2.5%, resting on a labor productivity growth rate in the 1.2% range, and a NAIRU of about 5.5%. Yet this prevailing consensus proved to be wrong—during the next five years, the economy outperformed the administration's forecasts by a considerable margin.

But in January 1995, despite passage of Clinton's budget plan in August 1993 and the stronger than expected economic conditions it fostered, projected budget deficits were still increasing, albeit at a slower pace, and the new Republican controlled Congress was demanding an administration plan to balance the budget within 7 years. As the underlying economic forecasts improved, CEA helped craft a new administration plan to achieve balance within 10 years without economically indefensible cuts in spending in priority areas including health care, education, infrastructure and research. The administration's plan was rejected by Congress, which used government shutdowns and threats of default on the federal debt to force the administration's hand. These tactics failed and in 1996, the administration and Congress agreed instead on a modest budget package that funded the government at current-law levels.

The economy continued to outperform forecasts, and CEA worked with President Clinton to develop a plan to balance the budget in 5 years. He announced the plan in February 1997 shortly after his re-election. Critics accused the President of "flip flopping" on the budget, but what had changed was not his fiscal policy stance, but the surprisingly strong economic conditions that resulted in larger than expected projected reductions in the deficit. Indeed, as the President and Congress worked toward a 5-year balanced budget deal in the spring of 1997, the Congressional Budget Office (CBO) announced that it was reducing its 5-year deficit projection by another $225 billion. Over the entire period between 1994 and 2000, actual budget outcomes were about $2.6 trillion better than those projected by the CBO in 1993, with CBO's estimates showing that stronger than expected economic conditions accounted for about 38 percent of this improvement with policy changes accounting for another 25 percent. Since CBO's estimates did not include the effects of these policy changes on aggregate economic performance, its estimate of their contribution to the improving budgetary outlook should be interpreted as a lower bound estimate of their actual effects.[1]

An economic boom that far exceeded forecasts was a major factor behind the remarkable budgetary improvement. But what explains the economy's extraordinary performance—a growth rate in excess of 3.8%, a labor productivity growth rate at 3%, nearly double the 1975-1995 rate, and an unemployment rate falling to 4% with low inflation at 2.6%—a combination of macroeconomic outcomes unfathomable when President Clinton took office? And what was the role of his policies in fostering this performance?

The most important economic variable underlying budget outcomes is the rate of growth, and a key volatile and unpredictable driver of economic growth is the productivity growth rate. In standard economic models, there are two main sources of labor productivity growth—capital deepening and technological progress. Both were in overdrive in the late 1990s.

As the 1995 *Economic Report* pointed out, there is a strong correlation between investment rates and labor productivity growth across industrial countries, and business investment soared in the US during the 1995-2000 period. President Clinton's fiscal policies were premised on an untested theory that a credible sustained reduction in the budget deficit would increase national savings, resulting in a significant decline in long-term interest rates that in turn would boost investment spending. The economy's performance during the second half of the 1990s was consistent with the theory's predictions: as the projected borrowing needs of the Federal Government declined, national savings increased, and long-term interest rates continued their gradual decline. Lower borrowing costs in turn fuelled stronger investment spending.

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[1] Douglas Elmendorf, Jeffrey Liebman and David Wilcox. 2002. "Fiscal Policy and Social Security Policy during the 1990s." In Jeffrey Frankel and Peter Orszag, eds. *American Economic Policy in the 1990s*. Cambridge: MIT Press. 61-119.

But this was only part of the story. The boom in information technology along with the resulting lower cost of computers and IT capital also fed the surge in business investment as did the soaring stock market.[2] As the anticipated productivity benefits of the 50-year old computer revolution began to intensify and spread throughout the economy, businesses were motivated to invest to reap these benefits.

The economy also benefitted from other unpredicted and unpredictable positive supply shocks, including a deceleration in health care costs in 1994-1995, moderate wage settlements, falling oil prices, and a soaring dollar. All of these beneficial developments ameliorated the predicted tradeoff between strong growth and low unemployment on the one hand and low inflation on the other.

As a result, the Federal Reserve—whose independence was staunchly defended by the Clinton economic team—was able to pursue a monetary policy that focused on the growth side of its dual mandate. Indeed, Federal Reserve Chairman Greenspan often mentioned positive productivity surprises in his explanation of Fed policy during the second half of the 1990s. And consistent with economic theory, the combination of tighter fiscal policy and relatively easy monetary policy held down real interest rates and created a macroeconomic climate that supported a growth-enhancing investment boom.

I have met former President Clinton many times since 2001 when his term of office ended. With a touch of humor, he often reminds me that as CEA Chair I provided forecasts that significantly underestimated the economy's macro performance. I humbly respond that I was simply providing unbiased forecasts based on the prevailing consensus among economists, a consensus that was proven wrong. I also remind him that as an economic forecaster and policy-maker it is wise to err on the side of caution.

[2] Alan Blinder and Janet Yellen. 2001. *The Fabulous Decade: Macroeconomic Lessons from the 1990s*, New York: The Century Foundation Press.

policy. By the early 1980s, the focus on macroeconomic stabilization policy had shifted to the Federal Reserve, and the economics profession had come to see a smaller role for discretionary countercyclical fiscal policy. However, this has changed again in recent years, as the length and severity of the Great Recession and its aftermath have precipitated a resurgence of interest in discretionary fiscal policy.

In addition, the Federal Government now plays a larger regulatory role in areas including health care, the environment, and labor markets than it did when CEA was first formed—a time before the establishment of, for example, the Environmental Protection Agency, the Department of Health and Human Services, the Department of Transportation, the Department of Education, and the Occupational Safety and Health Administration. At the same time, the field of economics has broadened to include not only traditional areas like macroeconomics and finance, but also subjects such as health care and the environment. As a result, a considerably larger fraction of CEA's work today is devoted to analyzing regulatory issues in areas like health, labor, and the environment than during its early years.

Despite the evolution in CEA's institutional structure and policy priorities over the years, CEA has continued to fulfill its functions under the Employment Act, which—as outlined above—can be understood as being organized around four interconnected functions: (1) helping to develop economic policy; (2) helping to advance the President's economic agenda; (3) gathering, analyzing, and interpreting information on economic trends and developments; and (4) engaging with the economics community. Of course, these functions overlap to some extent—for example, monitoring economic trends and engaging the economics community help to inform the formulation of economic policies. Yet examining how CEA has fulfilled these four functions over the course of its history is useful both for understanding how its work supports the President, and for illustrating certain characteristics which have helped to render it a more effective and durable institution.

Help to Develop Economic Policy

The Employment Act provides that CEA shall "develop and recommend to the President national economic policies to foster and promote free competitive enterprise, to avoid economic fluctuations or to diminish the effects thereof, and to maintain employment, production, and purchasing power." CEA performs many different tasks to fulfill this function, including working collaboratively with other offices and agencies to develop legislative proposals (such as the President's Budget and State of the Union initiatives), providing analysis to support regulatory processes, and supporting other administrative initiatives.

Although the Employment Act signaled that the Federal Government would be held responsible for how the economy functioned, its language reflected a careful balance between supporting macroeconomic management as well as a less active approach to the business cycle. As a result, CEA is not tied to one macroeconomic philosophy, but instead has "march[ed] alternately under these two banners" over the course of its history (Hargrove and Morley 1984).

The perspective of CEA has varied depending on the ideology of different administrations, the particular people chosen as chair, members and staff of the Council, the understanding of the economics profession more broadly, and the specific economic circumstances facing the country. However, CEA has consistently advanced a perspective that emphasizes the importance of decentralized decisions to the effective functioning of our market economy, but which also recognizes that the Federal Government has an important role in macroeconomic stabilization, in correcting market failures, and in ensuring that everyone participates sufficiently in the economy's benefits. Indeed, the Council's very first *Report* rejected both complete laissez-faire and overreliance on fiscal and monetary remedies as approaches to macroeconomic policy, denoting these two positions, respectively, as the "Spartan Doctrine of Laissez Faire" and the "Roman Doctrine of an External Remedy" (CEA 1946).

Keyserling and "Full-Employment Economics"

Perhaps the closest CEA has ever come to endorsing the "Roman" view was during the Truman Administration, when CEA was chaired by Leon Keyserling, the second person to hold that position. Before becoming CEA chairman, Keyserling had served as vice chairman of CEA and had previously worked as a legislative assistant on Capitol Hill, where he helped author, among other things, the Employment Act of 1946. Keyserling was influenced by proto-Keynesian theories, and became a major advocate of "full-employment economics—harnessing government spending to foster employment by creating demand and promoting consumer spending" (Wehrle 2004). Keyserling believed, "despite the grim experience of the 1930s, that the potential of the American economy was unlimited, and that with the proper combination of countercyclical and long-term economic policy, economic growth could produce and maintain abundance for all" (Brazelton 1997).

Unable to find political support for dramatically expanding domestic social programs, an increasingly frustrated Keyserling turned to defense spending as a means to advance his full-employment agenda. After Russia detonated an atomic bomb in August 1949, President Truman ordered that the State and Defense departments conduct a review of the national security situation and develop a planning document, which eventually became known as NSC 68. When war broke out in Korea, the Truman Administration definitively committed to the rapid mobilization of military resources called for in NSC 68.

While Keyserling was not a central figure in directing the mobilization effort, he actively promoted it and defended its economic viability.

Keyserling and the Council participated in the National Security Council's so-called "costing exercise" to estimate the cost of the military mobilization. CEA also helped to draft the economics chapter of NSC 68, and CEA defended the economic feasibility of a massive defense expansion against the view—held by the Secretary of Defense and the Budget Director—that it would precipitate "ruinous inflation, intolerable economic dislocation, or both" (Flash 1965). Keyserling also helped to forestall the implementation of direct price controls, believing they would dampen expanded production. In doing all of this, the Council helped to persuade policymakers that the Truman Administration's national security objectives were compatible with its economic ones.

For a few years, Keyserling successfully used the Korean War mobilization to promote his expansionist agenda. During the war, unemployment fell below 4 percent, and labor leaders appointed by Truman to various planning agencies helped to redirect some military spending to economically depressed regions and industries in the United States (Wehrle 2004).

By the end of the Korean War, however, Keyserling's influence, and support for his policies, had diminished. As inflation began to mount, the Council found itself torn between competing objectives: Keyserling warned the President about inflationary pressure, yet he also worried that excessive focus on inflation would be used as a pretext to dampen spending. This ambivalence served to exacerbate confusion within the administration about the proper course of action, and in turn, undercut the Council's influence toward the end of the Truman Presidency (Flash 1965).

The Heller Council and the 1964 Tax Cut

Another particularly notable instance where CEA played a large role in advocating for countercyclical policy occurred during the Kennedy and Johnson Administrations. In the early months of Kennedy's Presidency, unemployment had reached almost 7 percent and economic growth had been lackluster. Two schools of thought developed on the source of the problem: the first group, which included CEA Chairman Walter Heller, argued that the problem was insufficient aggregate demand, and that public spending or tax reductions were necessary to boost demand for goods and services; by contrast, the second group argued that there were structural deficiencies in the economy, and that increasing spending would only aggravate the problem (Norton 1977).

Drawing on relatively new macroeconomic concepts such as the fiscal multiplier and the full employment surplus, CEA made the case that the economy suffered from insufficient demand, emphasizing "the gap between progress and potential, the resistance to improvement of unemployment, and the drag of the wartime tax structure" (Flash 1965). The Council presented its argument publicly on several occasions: before the Joint Economic Committee in 1961, and in the 1962 and 1963 *Economic Report of the President*. In the 1963 *Economic Report*, the Council strongly advocated for a tax cut to boost demand:

> *[F]or all its advances, the Nation is still falling substantially short of its economic potential … Private initiative and public policy must join hands to break the barriers built up by the years of slack since 1957 and bring the Nation into a new period of sustained full employment and rapid economic growth … The main block to full employment is an unrealistically heavy burden of taxation. The time has come to remove it.*

Through these efforts, CEA helped solidify support for the tax reduction. President John F. Kennedy pushed for it in his 1963 State of the Union address, and it was ultimately signed into law by President Lyndon B. Johnson in 1964. CEA did not design the specific details of the tax reduction, but it helped to make the supporting economic case.

Edward Flash, a scholar of public administration, argues that this moment constituted a turning point in the Council's history by helping to align economic policymaking with economic thinking at that time:

> *As demonstrated by the Administration's tax program, the primary significance of the Heller Council is that it was the most important single creative force in the development of a new approach to economic policy. As the Employment Act of 1946 ratified the government's responsibility for the nation's economic welfare (and hence its acceptance of Keynesian principles), the tax proposals of 1963 signaled the policy-maker's recognition that expenditure-revenue combinations leading to deficits can be a constructive force in economic growth. Policy thinking became more consistent with economic thinking. A new tradition was established. The Council analyzed, advocated, articulated, and gained acceptance for new economic values, new techniques of economic analysis, and new concepts of fiscal policy as a positive contributor to national economic well-being (1965).*

Moreover, Flash notes that winning President Kennedy's approval for implementing countercyclical policy at a time of existing budget deficits was a notable achievement, especially considering that the President had previously committed himself to balancing the Federal budget.

Countercyclical Policy in Other Administrations

CEA has engaged in deliberations about countercyclical fiscal policy at some point during most administrations in the post-World War II era. As discussed later, CEA Chairman Arthur F. Burns helped to convince President Dwight D. Eisenhower to support counter-recessionary tax cuts, “the first time massive tax cuts were made at a time of Federal budgetary deficit to counter a recession” (Norton 1977). The Gardner Ackley CEA tried but failed to convince President Johnson to raise taxes in 1965 to avoid inflation. The Alan Greenspan CEA advocated for, and the Ford Administration proposed, a fiscal stimulus in 1975 that was considerably more moderate than what was ultimately enacted by Congress, and called for “greater fiscal restraint” in the 1976 *Economic Report* (CEA 1976). The Schultze CEA advocated for an additional stimulus in 1977 during the Carter Administration (Schultze 1996), while the Michael J. Boskin CEA advocated for set of tax measures to stimulate the economy during the George H.W. Bush Administration (Frankel 2003). The Laura D. Tyson CEA advocated for a small one-time expenditure stimulus as part of a larger deficit reduction program during the Clinton Administration. The R. Glenn Hubbard, N. Gregory Mankiw, and Harvey S. Rosen CEAs promoted tax cuts enacted in 2001 and 2003 as a means of stimulating the economy during a period of sluggish economic activity (CEA 2002; CEA 2004; Rosen and Forbes 2005).

Most recently, under the leadership of CEA Chairs Edward Lazear, Christina Romer, and Austan Goolsbee, CEA played a role in designing countercyclical measures that were passed in response to the 2008-09 global financial crisis and its aftermath. The Council conducted the overall macroeconomic analysis that helped identify the need for, and design of, countercyclical fiscal measures, most notably the American Recovery and Reinvestment Act of 2009 (see Box 7-2 for former CEA Chair Christina Romer’s account of the role that CEA played in the Obama Administration’s response to the financial crisis).

CEA has also pushed to defend existing automatic stabilizers—features of the tax and transfer system that automatically offset fluctuations in economic activity—against policy changes, such as balanced-budget proposals, that would interfere with them. Charles Schultze observes that “[w]hile most Republican CEAs throughout the period continued to be more cautious than their Democratic counterparts about the advice they gave on the use of fiscal policy for stabilization purposes, the difference was one of degree, not of kind” (1996).

Box 7-2: Former CEA Chair Christina Romer (2009 – 2010)

President Obama was elected in the middle of the severe financial crisis in November 2008. Even with incomplete data and rapidly changing conditions, it was clear at the time that the crisis was having a rapid and disastrous impact on the rest of the economy. Firms unable to get loans were laying off workers, consumers were deserting stores, and unemployed families were struggling to keep their homes.

Because of the crisis, the incoming economics team had to start designing many of the policy responses during the transition—before we had the resources or the skills of the professional staffs at our agencies. That was certainly true of the fiscal stimulus package that the President worked closely with Congress to craft, and which was signed into law as the American Recovery and Reinvestment Act less than a month after his inauguration. From late November on, the economics team debated and planned a package of tax cuts, infrastructure spending, and aid to those directly affected by the crisis to try to help stabilize the economy and make it stronger in the future.

Though we were a skeletal team—just the member nominees and two graduate students who would eventually become staff economists—the transition Council of Economic Advisers attempted to do what CEA always does: bring the best evidence and economic analysis to bear on the problem. We gathered economic projections from a wide range of public- and private-sector forecasters. In the spirit of bipartisan professionalism that has always characterized CEA, the outgoing chair, Edward Lazear, and his staff shared the evidence they had about the economy and where it was heading. We also collected the best estimates available of the likely effects of different types of fiscal actions from the economics literature, professional agencies such as the Federal Reserve, and private forecasters.

As we put the forecasts and the estimates of the effects of fiscal stimulus together, it quickly became apparent that the fiscal packages being considered by most analysts and Congress were too small. This was a once-in-a-century problem that required a once-in-a-century response. The analysis we presented to the President-Elect in mid-December 2008 helped persuade him to work with Congress for a larger, more effective package. Though the final legislation was still not has large as the President would have desired given the terrible recession, at $787 billion, the American Recovery and Reinvestment Act was by far the largest discretionary fiscal stimulus in American history. And a burgeoning literature on its effects confirms that the Act was essential in helping to halt the decline and turn the economy around.

In designing the Recovery Act, one component around which there was substantial uncertainty was aid to State and local governments. Rising unemployment was devastating state tax revenues, and economists feared that state balanced-budget requirements would force State and local governments to cut spending and employment just as their economies and citizens needed those funds and jobs the most. For this reason, the incoming economics team urged Congress to include in the Recovery Act transfers from the Federal Government to the States to stabilize their coffers. As a practical matter, this was accomplished primarily by temporarily increasing the fraction of Medicaid spending (always a joint Federal/State program) covered by the Federal Government. The final Recovery Act included roughly $140 billion of state fiscal relief of this and other sorts.

Though the logic of the action was sound, because such fiscal transfers are rare there was only limited empirical evidence on their likely effects. CEA helped fill that knowledge gap by doing a careful study of the state fiscal relief done through the Recovery Act. The study, conducted by four CEA staff economists, was included in CEA's first quarterly report to Congress on the effects of the Recovery Act. CEA economists used the fact that some of the variation in the fiscal relief across States was due to pre-existing differences in the generosity of their Medicaid programs, rather than to state economic conditions, to accurately identify the employment effects of these transfers. The estimates indicated that the effects were substantial. Indeed, the estimated job effects were sufficiently large that the state fiscal relief appeared to be one of the most cost-effective components of the legislation. The four economists ultimately expanded their study into a paper, which was published in the *American Economic Journal: Economic Policy* (where it won the best paper prize in 2013).[1]

This CEA analysis of state fiscal relief was influential in subsequent policy discussions and recommendations. Though the American economy started growing again in the summer of 2009, job losses continued throughout the year and unemployment remained painfully high. The economics team debated at length the relative merits of many measures to spur job growth. Interestingly, about the only thing we *didn't* debate was the desirability of additional state fiscal relief. What had been a logical but untested action in the Recovery Act was now understood to have been an effective job-creation tool—thanks in part to CEA's analysis. There was easy agreement that it belonged in any second comprehensive

[1] Gabriel Chodorow-Reich, Laura Feiveson, Zachary Liscow, and William Gui Woolston. 2012. "Does State Fiscal Relief During Recessions Increase Employment? Evidence from the American Recovery and Reinvestment Act." *American Economic Journal: Economic Policy* 4(3): 118–145.

jobs package. And in early December 2009, President Obama proposed additional action, which included further funds for State and local governments as a significant part.

Sadly, Congress did not accept all of the President's recommendations, and fewer additional job creation measures were taken that winter than were needed. But additional state fiscal relief resurfaced in a more limited form in a bill the President signed on August 10, 2010. As part of a multi-faceted act, Congress appropriated $10 billion in aid to State and local governments to help maintain teacher jobs. A treasured memento of my time at CEA is one of the pens the President used to sign that bill. It is a reminder that rigorous empirical analysis by one of the smallest agencies in Washington can sometimes spur legislation that creates jobs and helps heal a troubled economy.

Microeconomic Policy

In recent decades, CEA has increasingly spent its time applying core microeconomic lessons: that individuals and organizations' behavior is shaped by the incentives they face; that markets are generally an efficient way of organizing economic activity; that public policy can sometimes improve the functioning of markets, such as in the presence of externalities (when the market does not fully take social costs and benefits into account) or informational problems; and that policy choices can affect whether the benefits of markets are narrowly or broadly shared. Schultze writes that "the injection of basic microeconomic principles, well back from the frontiers of research, can significantly raise the quality of the debate" (1996).

Although CEA's views on some particular microeconomic issues have evolved over time and with administrations, this shared commitment to a basic microeconomic canon has ensured a substantial amount of continuity. Under both Republican and Democratic administrations, the Council has argued that reshaping incentives is often a better way of addressing market failures than imposing command-and-control regulation. It has also pushed for policies that promote overall economic efficiency, rather than the well-being of specific sectors, industries, or firms. Charles Schultze notes that "despite some areas of disagreement, a succession of CEAs under both parties has given similar advice on a wide range of microeconomic matters" (1996).

CEA has also frequently provided more detailed technical or empirical expertise, such as analyzing the effect of policies on incentives or performing cost-benefit analyses. Former CEA Chairman Joseph Stiglitz enumerates a number of specific "narrow microeconomic initiatives" in which CEA has played an important role, such as designing tradable permits in pollutants, incorporating risk and discounting into cost-benefit analysis, and introducing auction mechanisms (1997). During negotiations over the Clean Air Act Amendments of 1990, CEA was viewed as the "repository of neutral competence" and was called on to produce unbiased cost estimates of a range of different provisions (Porter 1997). In recent years, empirical research has become an especially important part of CEA's portfolio, reflecting the proliferation of available data and the economics profession's shift toward empirical work. This trend has benefited the field of microeconomics in particular (Stevenson 2014).

CEA has also helped to advocate for, or contribute to, the generation of new policy proposals. For example, the Burns Council supported the Federal Aid Highway Act of 1954, which began the present Interstate Highway System. The Heller Council under Presidents Kennedy and Johnson was especially prolific, "helping to shape transportation and trade bills, aiding in the development of the monetary 'twist' policy, helping to keep mortgage rates down, [and] developing the rationale of the wage-price guideposts" (Flash 1965). It also helped to develop the idea of the War on Poverty.[3] Other CEAs have helped to initiate or push for (sometimes successfully; sometimes not) various other reforms, such spectrum auctions, pension simplification and indexed bonds, reforms of the air-traffic control system, housing sector reform, and a comprehensive approach to natural-disaster policy (Stiglitz 1997). During the negotiations over the Kyoto Protocol on Climate Change, former CEA Chair Janet Yellen testified on a number of occasions regarding the cost savings that could be achieved through emissions trading and participation by developing countries (Hahn and Stavins 2002). (See Box 7-3 for former CEA Chairman N. Gregory Mankiw's description of CEA's role in trying to reform Fannie Mae and Freddie Mac during the George W. Bush Administration.)

[3] Walter Heller gives the following account of the impetus for the War on Poverty: "Then around Christmas of 1962, [President Kennedy] read Dwight MacDonald's poverty articles in the New Yorker that helped get him started. Then he asked to see some other things that had been written… He asked to see these things, read them and was obviously deeply affected … So first of all I had Bob [Lampman] put together the things he had done—the best work on the subject in the United States—namely measuring what had happened to poverty, what the sources of poverty were, what groups were impacted, why people were mired in poverty. We gave Kennedy this factual account about in March of 1963. Then something triggered my political interest in it: in June it was said that some Republican group—I've forgotten which Republican policy committee—was going to zero in on the poverty problem. At that point I wrote my basic memo to Kennedy saying in effect, 'You really should have in your 1964 program an attack—(I didn't call it a war on poverty, but an attack)—on poverty, and here are the kinds of things that it might include. Unless you tell us not to, we're going to go ahead and work on them.' We worked on them through the summer and—this, I think is well known—the very last thing I talked to him about—three days before the assassination—was the poverty program, and he said, 'It's going to be part of my program.' We didn't know how big it was to be" (Hargrove and Morley 1984).

Box 7-3: Former CEA Chairman N. Gregory Mankiw (2003 – 2005)

Looking back at my experience as CEA chair, I am struck by the broad range of questions the Council had to confront. Should corporate dividends be taxed at the same rate as ordinary income? What effect does Chinese exchange-rate policy have on the American economy? How should accountants treat executive stock options when computing a company's earnings? Why aren't U.S. utilities building new nuclear power plants? How should "means" be defined when means-testing a Medicare entitlement? What is the best way for policymakers to help speed the nascent recovery from the dot-com collapse?

For a professional economist, working at CEA is both demanding and exhilarating. Confronting such a large range of issues is inevitably a learning experience—and one done in short order and with high stakes. It is a great honor to play a small part in trying to steer public policy in a better direction and thereby improve the lives of our fellow citizens.

With the benefit of hindsight, one issue from my time at CEA is particularly notable: the oversight of Fannie Mae and Freddie Mac. CEA was part of a White House team that tried to reform these government-sponsored enterprises (GSEs). We recognized that the GSEs were problematic. Their private goal of profit maximization did not mesh well with the implicit government guarantee of their debts.

In a speech I gave in November 2003 to a conference of bank supervisors, I described the situation as follows: "The enormous size of the mortgage-backed securities market means that any problems at the GSEs matter for the financial system as a whole. This risk is a systemic issue also because the debt obligations of the housing GSEs are widely held by other financial institutions. The importance of GSE debt in the portfolios of other financial entities means that even a small mistake in GSE risk management could have ripple effects throughout the financial system."

The administration sought legislation that would create and empower a more effective regulator. The regulator would have the authority to set both risk-based and minimum capital standards for GSEs; to review and, if appropriate, reject new GSE activities; and to wind down the affairs of a troubled GSE through receivership. We also wanted to make the GSEs less political. We recommended removing presidentially appointed directors from their boards and giving the regulator a permanent funding mechanism by allowing it to assess the GSEs rather than relying on the congressional appropriations process.

In the end, the administration failed in this effort, at least while I was there. Legislation to improve the oversight of Fannie and Freddie was enacted only in July 2008, well after the imbalances that led to the 2007-08 financial crisis had built up, making the problems apparent to everyone. In 2003 and 2004, with financial markets still placid, Fannie and Freddie had lots of friends in Congress (on both sides of the aisle) who blocked the White House's reform efforts. But we fought the good fight. And subsequent history shows, I believe, that we were on the right side of the issue.

Did CEA at the time foresee the housing boom and bust that unfolded over the next six years? No, of course not. But we did recognize the vulnerabilities of the GSEs, which were major players in the huge market for mortgage-backed securities. Would the proposed reforms have prevented the financial crisis? No, probably not. But they might have made it less severe and more manageable.

People often ask me whether it is frustrating to work in Washington, noting how hard it is to get anything done. Yes, in some ways, it is. This episode is only one example where our good policy (as my White House colleagues and I saw it) was subverted by an uncooperative legislature.

Yet, over time, I have come to appreciate that frustration for those in policy jobs is not a bug in the system but rather a feature. The founding fathers, in their great wisdom, built this tension into the system. In high school civics classes, it goes by the name "checks and balances."

A common lament is that there is too much gridlock in Washington, and maybe there is. But imagine that your least favorite candidate wins the next presidential election. Might you be grateful when the new President and his or her CEA chair become frustrated while trying to implement their new ideas for economic policy?

Ensuring that Policies are in the Public Interest

CEA also plays an important role in providing analyses to demonstrate that some policies, while superficially appealing or offering substantial benefits to particular sectors or firms, are not cost-effective or in the national interest. Joseph Stiglitz claims that "the money saved from just one of the many bad projects the CEA had helped stop … would have been enough to provide us with a permanent endowment" (1997). Former CEA Chairman Ben Bernanke also emphasized this function when describing economists' role in policymaking more generally, while at the same time emphasizing the limitations of economics:

> *Economics is a highly sophisticated field of thought that is superb at explaining to policymakers precisely why the choices they made in the past were wrong. About the future, not so much. However, careful economic analysis does have one important benefit, which is that it can help kill ideas that are completely logically inconsistent or wildly at variance with the data. This insight covers at least 90 percent of proposed economic policies (2013).*

Box 7-4: Former CEA Chairman Joseph Stiglitz (1995 – 1997)

My four years at the Council (two as a member and two as chairman) were perhaps the most memorable in my life. There were many battles—some which we won, some which we lost, some in which we achieved a temporary victory, and some which we lost in the short run only to see our positions vindicated with time. We came into government at an exciting time. The fall of the Iron Curtain had redefined the economic agenda. Our challenge was to find the right balance between the market and the state. The Council saw its role as helping to clarify the principles, and then applying these principles to the major issues of the day.

The Council of Economic Advisers had an important *positive* agenda, as we pushed to reshape trade, welfare, and environmental policies. To name one example, we successfully pushed for inflation indexed bonds, arguing that they could provide retirees with insurance against inflation—which they could not obtain in other ways—and that the risk premium that the market would likely pay for these bonds would generate revenues, important then as now in the context of budgetary constraints. Some opposed inflation indexed bonds, ostensibly because there would be little demand for them but perhaps grounded in the fact that the low turnover on such bonds meant they would generate few fees for Wall Street. Our view that there would be demand was vindicated and Treasury Inflation Protected Securities (TIPS) have proven to be a durable, useful, and informative part of the financial landscape.

Some of the most intense battles we fought now seem dated, and that may have been partly because of our success. Today, there is a broad consensus against "corporate welfare"—and especially tax expenditures that both distort the economy and increase inequality, even if they have shown enormous resilience. At the time, the topic was politically sensitive, but we drew up a list of them for the President, and that list has only gotten longer with time.

But we also did a lot to stop bad ideas and in collaboration with many allies across government, we succeeded in many arenas. We forged an alliance with the Antitrust Division of the Department of Justice to block a proposal to sustain the price of aluminum through the creation of a global aluminum cartel. We helped overcome legislative attempts to change the mandate of the Federal Reserve to focus only on inflation and not on unemployment, and helped defeat a constitutional amendment to require a balanced budget.

One temporary victory contains important lessons for CEA's commitment to understanding incentives. For years, we succeeded in blocking the privatization of the United States Enrichment Corporation

(USEC). USEC was responsible for producing and marketing enriched uranium, the key ingredient in nuclear power plants and in atomic bombs. CEA argued that private incentives to create markets for USEC's product conflicted with national and global interests in non-proliferation. Even worse, USEC was entrusted with bringing into the United States the enriched uranium from deactivated Russian warheads. We worried that USEC's profit-making incentives would induce them to do what they could to avoid bringing the uranium into the United States. CEA's concerns proved justified, as we uncovered that USEC had refused an offer to buy substantial amounts of uranium from Russia. This discovery halted the privatization, albeit only temporarily. But USEC's continued travails—leading even to proposals for renationalization—vindicated CEA's position.

The Council was also engaged in other international issues. We opposed the policy of Chinese containment that was pursued in the earliest days of the Clinton Administration, and when the administration changed course toward re-engagement, we became active participants in that process. Our expertise in the transition from Communism to a market economy, especially in Russia, gave us a seat at the table in discussions over policies in that part of the world.

The Council was actively engaged in trade policy, not just pushing back against protectionist measures but defining the *principles* that should guide market access initiatives. We questioned unfettered capital flows across borders, a view that has become "officially" vindicated by the IMF's endorsement of it.

As I think back over the years at the Council, one of the things that is striking is how many of the issues we focused on then have since risen to the top of the agenda. One was climate change. The Council was actively engaged in thinking about economic strategies that would reduce our emissions and those of the rest of the world. I served on the Intergovernmental Panel on Climate Change (which shared the 2007 Nobel Peace Prize with former Vice President Al Gore).

Another was inequality. We debated the causes and what could be done about it, and included a full chapter on the topic in the 1997 *Economic Report of the President*. Our analysis highlighted how reducing capital gains tax rates would enhance the country's already worsening inequality and further distort the economy.

As we engaged in these discussions and many more, CEA developed an enormously strong sense of comradery. It was these bonds as much as the ideas themselves that I think about when I reflect upon my four years at the Council.

There were many lessons that I draw from these and a multitude of other examples during my four years in the Council. The Council can stop bad ideas and initiate goods ones. Given its small—but highly dedicated—staff, it must be focused and use leverage. It is most effective when it works closely with other agencies, at multiple levels—interacting both with staff and top political appointees. This is even truer today, with an increasingly large number of departments having a chief economist. Not to sound too imperial, but economics and economic analysis enter into every aspect of public decision-making. Incentives matter. And this is true not just in the arena of domestic policy, but also foreign policy. Finally, most of the important issues are long run—whatever we do today, we will be dealing with them for years to come. The Council can play an important role in shaping, and elevating, the public debate.

As I wrote 20 years ago in celebration of the Council's 50th anniversary,[1] CEA is an important institutional innovation that has served the country well. Like other agencies in government, it has a "special interest," one that often gets short shrift in day-to-day political life: the national interest.

[1] Joseph Stiglitz. 1997. "Looking Out for the National Interest: The Principles of the Council of Economic Advisers." *American Economic Review* 87 (2): 109-113.

Some examples of this function are especially noteworthy (see Box 7 -4 for former CEA Chairman Joseph Stiglitz's account of CEA's role in evaluating and generating policy proposals during the Clinton Administration). For instance, the Heller Council argued against a proposal during the Kennedy Administration to use nuclear explosives to widen the Panama Canal. In the Nixon Administration, CEA played a leading role in the analysis that led to the conclusion that the government should not subsidize the development of a supersonic transport or SST plane, dubbed the "sure-to-be-subsidized transport" (Schultze 1996). Under President Ronald Reagan, CEA participated in a Gold Commission, which investigated the feasibility of returning to the gold standard, and ultimately advised against doing so.

Of course, the President makes policy decisions based on a wide range of other advice and perspectives, and economic considerations often are not paramount. Furthermore, as former CEA Chairman Herbert Stein points out, not all policy proposals lend themselves to such definitive economic conclusions:

> *The range of uncertainty [in economics] has been very great and the range of disagreements among respected people is very great. The political figure making a decision has this great range from which to choose, and he has to make a choice on some basis other than what*

can be reported to him as the perceived wisdom of the economics profession because that perceived wisdom gives pretty wide range (Hargrove and Morley 1984).

Finally, economic advice is only useful to policymakers if it is communicated well. Former CEA Chairman Martin Baily emphasizes that when CEA is assessing proposals from Congress or other parts of the administration, it is important for it "to frame those issues in a way that can help foster useful discussion among policymakers" (2006).

Help to Advance the President's Economic Agenda

Another primary function of CEA is to help advance the President's economic agenda. As outlined in CEA's 1961 statement before the Joint Economic Committee, "[t]he Council has a responsibility to explain to the Congress and to the public the general economic strategy of the President's program, especially as it relates to the objectives of the Employment Act." CEA accomplishes this through several different means: writing the annual *Economic Report of the President* and testifying before the Joint Economic Committee, producing reports on specific policy proposals or issues, delivering speeches, writing op-eds, speaking with reporters, and in more recent years, writing blog posts and engaging the public on social media outlets.

Despite the fact that CEA draws heavily from academia and performs economic research, it is not an academic institution or an independent body. Instead, CEA is part of the team that helps to develop the President's agenda—and its public communications are intended to complement that role, while reflecting rigorous economic research. Like communications from any other component of the Executive Office of the President or the administration more generally, statements from CEA are intended to be consistent with the President's agenda and economic policy.

As many commentators and former CEA chairs have observed, there can be a tension between CEA's duty to advance the President's agenda and its responsibility to provide expert economic advice. For most of its history, CEA has managed to strike a successful balance between these roles. As Edward Flash notes, CEA's reports are "not … partisan tracts but rather documents oriented to the economic policies and values of the Administration" (1965). However, there are inherent challenges entailed by fulfilling these dual responsibilities. This section uses the conflict between CEA's first chairman, Edwin G. Nourse, and its second, Leon H. Keyserling, to explore these challenges. It also draws some institutional lessons to ensure the Council's continued effectiveness.

Nourse and Keyserling

The three years (1946-49) during which Nourse and Keyserling served on the Council together were difficult ones. Nourse opposed Keyserling's "full-employment economics" and expansionist agenda, and held different views than Keyserling on inflation and countercyclical policy. Their disagreements on economic policy were exacerbated by ambiguity surrounding the Council's organizational structure. Although Nourse was the official chairman, he and the two members had functionally equivalent roles and responsibilities, and each of them got one vote when making decisions. Consequently, it was not always clear who was speaking on behalf of the Council, and Edward Flash reports that by 1948, "the Council could no longer report to the President in a single voice, as memoranda and reports began to incorporate differing individual viewpoints" (1965).

Nourse and Keyserling also held fundamentally different views about how the Council should operate. Nourse, who had enjoyed a distinguished career as an agricultural economist, viewed the Council as a "scientific agency" that should be objective and scrupulously avoid politics. Nourse summarized his view of the Council in a letter to President Truman accepting the offer of chairmanship:

> *The Council of Economic Advisers is conceived as a scientific agency of the Federal Government. Its prime function is to bring the best available methods of social science to the service of the Chief Executive and of the Congress in formulating national policy from year to year and from month to month. There is no occasion for the Council to become involved in any way in the advocacy of particular measures or in the rival beliefs and struggles of the different economic and political interest groups. It should give a clearer and more comprehensive picture than we have ever had as to the economic state of the nation, as to factors which are tending to retard prosperity, and as to the probable effect of various remedial measures which may be under consideration by the Executive or the Congress (Flash 1965).*

Nourse believed that the Council's function should be limited to providing advice, and did not view himself as "being an active participant in, or advocate of, the President's program, involved in day-to-day affairs, or in the promotion of his program" (Norton 1977). Indeed, he took this notion so seriously that he argued that members of the Council should not testify before any Congressional committees other than appropriation committees.

By contrast, Keyserling had actively engaged in public policy before arriving at CEA: he had served as a legislative assistant to Senator Robert Wagner and as a staff member of the Senate Committee on Banking and Currency, worked in different capacities at various public housing agencies, and participated in numerous Democratic election campaigns. He—and to a lesser extent, CEA's other member, John D. Clark—believed that the Council should not only provide advice, but also should participate in the policy process and advocate for the President's policies. As discussed above, for example, he did not hesitate to involve himself in the Korean War mobilization, since it aligned with his views of the necessity of economic expansion. In addition, he felt that the Council's advice should not be limited to economics, and should include "social and political aspects" as well (Norton 1977). Keyserling and Clark also thought it was entirely appropriate for them to testify before Congressional committees. Ultimately, it became necessary for President Truman to resolve the disagreement, siding with Keyserling and Clark.

After three years of service as chairman of CEA, Nourse tendered his resignation to President Truman. Nourse had become increasingly frustrated that he was "unable to develop satisfactory relations or channels of communication with the President and the White House," while Keyserling, who was more "operationally and promotionally included than Nourse," had an easier time operating within a political environment (Flash 1965). Keyserling was named chairman about six months after Nourse's departure.

Although Keyserling outlasted Nourse, the acrimony between the two men, along with the perception of Keyserling as being overly political, contributed to questions about the Council's future. Criticism began to intensify toward the later part of the Truman Administration, and in 1949, the Hoover Commission on Government Reorganization recommended that CEA be replaced with an Office of the Economic Adviser that would have a single head, but a similar staff (Nourse 1953).

Once Republicans won the White House and both houses of Congress in 1952, the future status of the Council was unclear. Toward the end of the Truman Administration, Congress cut the Council's budget for fiscal year 1953 by 25 percent, but a group of Senators who supported the Council managed to have its funds distributed so as to fully fund it for the first nine months of the fiscal year (Flash 1965). Funds ran out on March 1, 1953, around six weeks after President Dwight D. Eisenhower took office, by which time most of CEA's staff had dispersed. The new Congress refused President Eisenhower's request to extend funds for the end of the fiscal year, instead providing funding for a single economic assistant to the President (Porter 1991). It was "widely believed at the time that the Council's shut-down towards the end of the Truman Administration was a result of excess politicking under Keyserling's chairmanship" (Naveh 1981), though Keyserling himself disputed this perception.

Eventually, Arthur F. Burns, who had been appointed as President Eisenhower's sole economic adviser, convinced the President and Congress to keep CEA, arguing that "the President definitely needed economic advice on a continual basis and on a professional level … [and] that a deliberative body would serve the President better than a single economic adviser" (Hargrove and Morley 1984). Congress restored CEA's appropriation and Burns was sworn in as chairman in March 1953.

Burns also helped to persuade President Eisenhower to reorganize CEA. Together with staff from the Budget Bureau (the precursor to the Office of Management and Budget), he worked to develop Reorganization Plan No. 9, which formally established the chair as the leader of CEA, and gave her or him responsibility for representing the Council to the President. However, Hugh Norton writes that perhaps Burns's greatest "contribution was his success, at least in appearance, in removing the Council from the area of partisanship into which it had fallen in the late Truman-Keyserling period … To what degree this was merely an illusion is debatable, but at least he created the image" (1977).

Institutional Lessons

The discord between Nourse and Keyserling and its political fall-out illustrates that CEA chairs and members need to be able to operate effectively within a political environment without it affecting the integrity of their economic advice. Put more succinctly, Charles Schultze advises that "CEA members should see themselves as partisan advocates of the efficient solution" (1996). Former CEA Chairman Murray Weidenbaum writes that subsequent CEA chairs and members have "tried to avoid the two extremes of the Truman Administration so as not to be pegged as either advocate or oracle" (1996).

Political values and judgments intersect with CEA's role in a number of ways. As Schultze notes, CEA must have some political sensibilities to be effective: "[t]he CEA chairman and members cannot be effective if they are seen as political eunuchs, with little understanding of the political stakes involved" (1996). Arthur Okun concurs, "[i]t is far more important for society and for the profession to have economists who maintain rapport with the President and thus have the greatest influence on the inside" (Naveh 1981). Similarly, former CEA Member William A. Niskanen recommends that "[m]embers of the CEA, and other senior policy advisers, should be selected on the basis of three criteria: professionalism, loyalty to the fundamental goals of the government in their area of responsibility, and an ability to operate in a political environment" (1986).

Moreover, although CEA's strength is providing unvarnished economic advice, it is impossible to divorce this advice from the broader context of the Administration's goals and objectives. While economists can help policymakers to weigh tradeoffs among different policy options or to design policies so that they are more likely to achieve their stated objective, how those tradeoffs are weighed and goals are set often depends on values. In addition, policy recommendations themselves are more relevant if they can be implemented, which in turn depends on a range of political factors like legislative feasibility and how the policy is described and contextualized. Finally, CEA chairs are selected and agree to serve because they at least broadly share the goals and values of the President and the administration. Beyond the chair, however, there is no guarantee that CEA members, or especially staff economists and researchers, share a political or philosophical agreement with the President.

As dictated in the Employment Act of 1946, CEA's advice must ultimately be guided by its own analysis of which economic policies will foster and promote free competitive enterprise, avoid economic fluctuations, and maintain employment, production, and purchasing power. Former CEA chairs, members, and staff offer several specific pieces of advice as to how to successfully strike this balance: they advise that CEA should not publicly advocate for policies that are not supported by economic analysis, and that CEA should stick to giving economic advice, not political advice. CEA's comparative advantage is economics, and as illustrated by Keyserling's tenure and its aftermath, straying outside this function risks damaging the institution's credibility.

Others advise that the Council should not get too involved in policy coordination. CEA's limited staff and resources, combined with the academic background of most of its staff, render it poorly equipped to serve as a policy coordinating body. One episode that illustrates this lesson occurred during the Johnson Administration, when CEA was responsible for the day-to-day administration of wage-price guideposts to combat inflation. Reflecting on the experience, Walter Heller remarked that there was no other appropriate agency to handle the wage-price guideposts, but that it was "diversionary" and that "the Council has to stay away from that kind of operational responsibility" (Hargrove and Morley 1984).

Excessive involvement in policy coordination can also have the effect of undermining CEA's institutional credibility, due to the types of compromises that are necessary. Hugh Norton writes that CEA's efforts to administer the wage-price guidelines "had the effect of weakening the general moral authority of the Council" (1977). Charles Schultze refused to move his office from the Eisenhower Executive Office Building to the West Wing and serve as an economic policy coordinator because "[h]e felt it would compromise his objectivity and burden him with administrative duties inconsistent with his role as the head of the President's in-house economic think tank" (Eizenstat 1992). Stuart Eizenstat, President Carter's domestic policy adviser, argues that "[t]he CEA cannot provide both detached, Olympian economic advice and become enmeshed in the daily, inter-agency compromises and political log-rolling" (1992).

This is not to say that CEA should not contribute to operational matters at all. To the contrary, it is quite common for CEA to participate in interagency committees, and CEA occasionally even chairs some committees. Yet the academic background of most of CEA's staff and its mission to provide expert economic advice, render it unsuited to serve as a policy or strategic coordinator.

Recognizing this, most recent Presidents have relied on some other institutional body or senior White House aides to coordinate economic policy.[4] Since 1993, the National Economic Council has been responsible for coordinating economic policymaking. These arrangements have largely served to augment CEA's effectiveness by permitting it to focus on providing economic advice and analysis and giving the Council greater exposure to the President. Roger Porter writes:

> *What might appear on the surface as a competitive arrangement has rarely been viewed by the participants as a zero-sum game. To the contrary, both the CEA chairman and the White House economic-policy assistant have usually viewed the other as an ally and often as a trusted confidant (1997).*

Former CEA Chairman Alan Krueger writes that the development of the National Economic Council "elevated the Council of Economic Advisers, freeing it to advocate efficient economic programs and ensuring that the [P]resident had its input" (2000).

[4] For example, President Eisenhower established the Advisory Board on Economic Growth and Stability and the Council on Foreign Economic Policy; President Nixon created the Cabinet Committee on Economic Policy, the Council on International Economic Policy, and the Council on Economic Policy; President Ford established the Economic Policy Board; President Carter created the Economic Policy Group; and President Reagan established the Economic Policy Council. Most of these committees or councils have not continued in the same form from one administration to the next (Orszag et al. 2002; Porter 1983).

Gather, Analyze, and Interpret Information on Economic Trends and Developments

Another one of CEA's functions under the Employment Act of 1946 is to "to gather timely and authoritative information concerning economic developments and economic trends." This includes staying up to date on major trends in the macroeconomy, financial markets, and labor markets, as well as in sectors such as health care, energy, and housing. This role is important not only because developments in these sectors can be the bases for motivating future policies, but also because the President, senior White House staff, and the public need to understand these issues.

CEA fulfills this role through a variety of different means, including: sending regular memos to the President on the evening before key data releases; providing daily, weekly, or monthly updates on developments in the economy; writing more detailed one-off memos to the President and the senior White House team on specific issues; producing public reports on relevant economic topics or trends; and publishing the annual *Economic Report of the President*. Sometimes, the President will call for CEA to explicate a particular issue. For example, Murray Weidenbaum reports having a "pleasant—but spirited and extended—difference of views [with President Ronald Reagan] on the matter of seasonally adjusted versus unadjusted reports on employment and unemployment" (1988). In many cases, this work does not immediately motivate or advance a particular policy, but the ongoing monitoring and communicating information about the economy ultimately helps to inform the development, prioritization, and public reception of economic policies (see Box 7-5 for former CEA Chairman Alan Greenspan's history of the weekly Gross National Product measurement that CEA developed and used to assess the need for expansionary fiscal measures during the Ford Administration).

The Burns Council and the 1953-54 Recession

The 1953-54 recession represented an early test of this information-gathering function. By the time President Eisenhower took office in 1953, the economy had fully recovered from a mild recession that had occurred a few years earlier, and the unemployment rate was at its lowest point since World War II. However, in July 1953, the United States signed the Korean armistice, and the public anticipated that a substantial decline in military expenditures would soon follow, sparking concern about an impending recession (Engelbourg 1980).

During the summer of 1953, the newly reconstituted Council grew increasingly worried about the possibility of a recession, and spent the next

Box 7-5: Former CEA Chairman Alan Greenspan (1974 – 1977)

In the autumn of 1974, industrial production began to fall rapidly, and unemployment started to increase rapidly. That the economy was heading into a recession (if it were not in fact already in one) didn't require much debate. By Christmas, the key question for the Ford Administration's economic policy was whether we were experiencing an inventory recession, which would mean a sharp but temporary erosion in production and employment as businesses worked off excess inventories, or a far more dangerous softening in the economy engendered by a persistent weakness in final demand. This was the burning issue for the President. For a short-term inventory correction, the optimum policy, as we saw it, was to do as little as politically possible.

The political advice being offered to the administration was unequivocal. It was typified by the March 1975 testimony of AFL-CIO president George Meany to Congress that "America is in the worst economic emergency since the Great Depression … The situation is frightening now and it is growing more ominous by the day. This is not just another recession, for it has no parallel in the five recessions in the post–World War II period. America is far beyond the point where the situation can correct itself. Massive government action is needed."

The Council of Economic Advisers had no real time measure of the state of demand and inventories. Official estimates of gross national product (GNP) and its components would answer the vexing question. But the data required to make the key policy choices would become available weeks, perhaps months, in the future. In December 1974, however, CEA developed what amounted to a weekly GNP. It would not have passed the exacting statistical publication standards of the Bureau of Economic Analysis of the Department of Commerce, but it was more than adequate—in fact, quite instrumental—in answering the question of whether we were experiencing an inventory recession, a final demand recession, or both.

While the Department of Commerce has since abandoned its weekly retail sales series, it nonetheless did yeoman service during that period in indicating that personal consumption expenditures were not undergoing a downward plunge. This was confirmed by the timely 10-day data of full coverage of motor vehicle sales. The other sectors of the economy had to be estimated more indirectly. Industry trade sources, coupled with the latest data on building permits (which leads residential construction) outlined the residential sector for us. Survey forecasts of plant and equipment, monthly new orders and shipments for machinery, data on nonresidential construction, and, with a delay, imports of capital equipment constructed a crude proxy for capital investment. From the unemployment insurance system we were able to develop a rough indicator of aggregate hours worked, which, combined with an estimate of output per work hour (which were little more than educated guesses), yielded a rough preliminary estimate of total real GNP, which was then adjusted to reconcile with its component parts.

These data indicated, with some degree of robustness, something that we knew for a fact only much later: that the rate of inventory liquidation—the gap between GNP and final demand—was exceptionally large by historic standards. That gap reflected the fact that production had been cut well below the level of final demand in order to work off the excess inventories that had accumulated. Therefore, if final demand continued to stabilize, as apparently it was doing in the early weeks of 1975, the recession's low point was close at hand and a marked rebound from the downturn was highly likely. Inventory liquidation cannot go on indefinitely. The rate must eventually slow, and that process closes the gap between final demand and production, sometimes quite rapidly.

It soon became clear from the weekly insured unemployment data and several qualitative indicators that the worst was over.[1] At that point we could conclude that further expansionary fiscal measures beyond the modest initiatives of the Ford Administration would be unnecessary and in the long run could turn out to be counterproductive. Short-term emergency GNP monitoring was no longer necessary and the short, but admirable, history of the weekly GNP came to a close.

[1] Real GDP rose 6.2 percent from Q1:1975 to Q1:1976.

few months documenting economic data showing worsening conditions. CEA's new chairman, Arthur Burns, was an expert on business cycles, and was considered to be "a champion of empirical, or inductive, economics, preferring to draw conclusions and base policy upon observable facts rather than deductively from theoretical relationships and models" (Flash 1965). Thus, over the next several months, the Council monitored various economic indicators, such as unemployment, stock prices, commercial construction, new housing starts, farm income, business inventory accumulation, and business sales, and submitted regular updates to the President and other agencies.

In addition to monitoring economic developments, the Council also began actively helping to develop a counter-recessionary strategy. First, the Council attempted to convince the Federal Reserve to ease the money supply and credit, and Burns "lost no opportunity to seek its cooperation" (Norton 1977). (Note that the Federal Reserve has long-established independence, and Executive Branch policy in recent administrations has been to not comment on or in any way attempt to influence its actions.) Second, CEA advocated for reducing Federal taxes to stimulate demand, contrary to the views of then-Treasury Secretary George Humphrey, who was concerned about tax cuts adding to the deficit.[5] Finally, CEA advocated for increased public works spending, developing various proposals and publicly calling for it in the 1954 *Economic Report of the President*. However, Burns recognized that public works projects would take a long time to implement and take effect, and the Council ultimately advised that extra public works funds should only be requested if unemployment reached six million in 1954, which never came close to occurring (Engelbourg 1980). Thus, although the Council and others within the administration devoted much deliberation to planning public works activities, in the end, their practical effects were fairly minimal.

In the end, the economy experienced a relatively short and mild recession, an outcome that helped CEA reach "a high-water mark of prestige and acceptance" (Flash 1965).[6] Moreover, as noted previously, this was the first time that a major tax cut had been implemented at the time of a budgetary shortfall to counter a recession. According to the 1966 *Economic Report of the President*, the administration's actions in 1954 established "the bipartisan character of expansionary fiscal policies … for the first time" (CEA 1966).

That being said, some have argued that the Council's work in monitoring and informing the administration and the public about economic developments was ultimately more influential than its direct efforts to promote specific countercyclical policies. Edward Flash writes:

> *Burns' inductive economics reinforced policy objectives and provided an excellent analysis of unfolding developments ... Except for underestimating the reductions in government expenditures for fiscal 1954 and allegedly overestimating administrative budget flexibility, the Council correctly assessed the mildness of the recession and provided*

[5] Only a couple years later, their roles in the debate were reversed. In 1956, Burns and Humphrey took opposite sides in another dispute, with Humphrey arguing for a tax reduction and Burns arguing against it, because inflation was beginning to pick up. Humphrey scheduled a meeting to make his case to President Eisenhower. Burns's account of the meeting is as follows: "Eisenhower greeted us with his customary enthusiasm: 'My two friends, just the two men I wanted to see. I just had a damn fool businessman in here saying that we ought to lower taxes now, this at a time when inflation is beginning to heat up—to lower taxes! Can you imagine any idiocy like that?' I took out a handkerchief and covered my face … It was all I could do to control myself from bursting out laughing. Well, there was talk about all kinds of things for about an hour and a quarter. I did not say one word. I was waiting for Humphrey; but he never got around to the subject of the meeting" (Hargrove and Morley 1984).

[6] Chairman Burns's efforts also won praise from President Eisenhower, with the President remarking to him one day, "Arthur, my boy, you would have made a fine chief of staff overseas during the war" (Norton 1977).

> *an informational basis for appropriate Administration policies. Through Burns, the Council kept the President and the Cabinet informed; through ABEGS [the Advisory Board on Economic Growth and Stability], chaired by Burns, the Council accomplished the same thing with departments and agencies. To the President, Burns provided constant and expert counsel; to the departments he conveyed an overview of recession developments and governmental countermoves that transcended particular operational operations and outlook (1965).*

By contrast, Flash argues that "it appears reasonable to conclude that … one, the Council's influence on the [F]ederal [G]overnment's actions of tax reduction and monetary easing which most significantly contributed to recovery was minor and two, those instances where its influence was significant involved actions that did not bulk large in recovery impact" (1965). For instance, he notes that much of the tax reduction that was enacted had already been scheduled to go into effect: the personal income tax reduction was implemented as a result of legislation enacted during the Korean War mobilization, and the excess profits tax was scheduled to expire automatically. CEA did persuade the President to pass an additional tax reduction of $1.4 billion, but by the time it was implemented, the recovery was already underway.

The 1970s and Stagflation

Of course, there have also been moments in CEA's history where its interpretation of economic trends and its understanding of the appropriate policy response have proved deficient. Herbert Stein notes that the 1970s were a particularly difficult time for CEA:

> *The later Nixon years, the Ford years and the Carter years were a period in which the CEA struggled with problems for which the economics profession was unprepared. High unemployment and high inflation persisted. Fiscal policy was dominated by concern with rising expenditures and deficits. The growth rate of potential output seemed to be slowing down for reasons that were not understood (1996).*

Stein writes that CEA's "most serious error" during the Nixon Administration was thinking that the natural rate of unemployment was 4 percent. This led the Council to think that it only had to let unemployment rise slightly above that before inflation would start to dissipate. Yet CEA was proven wrong, and when unemployment rose to 6 percent with no sign of progress, “confidence in the policy of ‘gradualism’ evaporated … [which] helped to set the stage for the radical move to price and wage controls, which the CEA had not foreseen and did not want” (1996).

More generally, Stein comments that two institutional deficiencies of CEA are that “it does not look far enough ahead, but gets too engrossed in immediate problems … [and that] like the government as a whole, is deficient in contingency planning.” To remedy the first problem, Stein advises that “[i]t might be useful to segregate a portion of the staff, under the guidance of one of the members, to think only of what the economy and its problems might look like in, say, 25 years” (1996).

Engage the Economics Community

The final function of CEA is to engage with the economics community, by staying abreast of the latest academic research and by sharing new insights with policymakers, and in turn, by communicating the administration’s actions and plans to the economics community. This function helps to support the administration’s efforts to develop economic policies and to articulate and advance the President’s agenda. While the academic character of CEA may not have been originally intended by Congress when it created CEA, this engagement has arguably made the Council a more effective and durable institution.

The Origins of Economists in the White House

Although CEA is now closely identified with the economics profession, this was not originally the case. J. Bradford DeLong writes that “[e]stablishing in the White House staff a group of short-term employees with a primary allegiance to economists’ sense of the public interest may have been the furthest thing from the minds of those who wrote Section 4 of the 1946 Employment Act” (1996). Rather, during the lead-up to the passage of the Employment Act, “[t]here were some people in Congress who envisioned the Council as a representative body … [and that] each one of the three basic sectors of the American economy; agriculture, industry and labor, should be represented on the Council” (Naveh 1981). Some supporters of the Employment Act wanted CEA to be staffed by people who had experience working in government or business, while others wanted to appoint academic economists.

In the end, the first CEA under President Truman included representation from all of these backgrounds. Nourse was an agricultural economist who had spent much of his career at the Brookings Institution; Keyserling was a lawyer who had completed graduate coursework in economics, and had experience working in government and ties to organized labor; and Clark was a former oil industry executive and a business school dean. By comparison, the staff recruited to serve on the first Council was comprised of "[e]conomists who integrated government experience and academic training" … almost all of whom "could be called government careerists" (Naveh 1981).

The shift toward hiring more academic economists commenced under the Burns Council, and intensified during the Heller Council. In part, Burns started hiring academic economists due to a scarcity of available labor: "Burns had a hard time finding qualified economists who at the same time, were not too closely identified with the previous administrations, would agree to work for President Eisenhower, [and] would stay in Washington at the time [of] Senator McCarthy's investigations." Meanwhile, academic institutions were a "convenient supplier of temporary personnel" (Naveh 1981). Burns also saw hiring academics as a means of depoliticizing CEA and establishing its credibility, which was especially important since CEA had come to be viewed as excessively political during Keyserling's tenure.

Institutional Advantages and Challenges

CEA's economic perspective and academic character have, as Burns intended, helped to insulate it against politics to some extent. As discussed above, the Council has held a number of the same positions under both Democratic and Republican administrations. In large part, this is because CEA tends to reflect the policy views of the economics profession, and on many (but not all) issues, "there is a distinct consensus among economists" (Schultze 1996). Murray Weidenbaum notes that when Congress in 1995 was debating whether to continue to fund CEA, "every active Republican ex-chairman came to the defense of the CEA as well as the Democratic economists who served on the [C]ouncil" (1996). When the administration changes, the leadership of CEA changes too, but there is a tradition of its staff continuing to serve through the first summer of the subsequent administration.

Some former CEA chairs have claimed that the institutional structure of CEA can help to reinforce its economic perspective. For example, Joseph Stiglitz argues that the fact that CEA is composed of "citizen-bureaucrats" who know they will be returning to their academic perches shortly means that they "have a long-term incentive to maintain [their] professional reputations" (1997), and that this creates an incentive for CEA staff to ensure that its recommendations are economically defensible. This point is echoed by former CEA Chairman Martin Feldstein (1992) and former CEA Member Jeffrey Frankel (2003). Of course, CEA's perspective is not unique,

Box 7-6: Former CEA Chairman Martin Feldstein (1982 – 1984)

I became Chairman of President Ronald Reagan's Council of Economic Advisers in the summer of 1982. I served for two years, the maximum time allowed by Harvard's policy of leave for government service. Acting as CEA chairman provided a crash course in a wide range of economic issues, including exchange rates, financial regulation and emerging market deficits, as well as an education in how the political process works inside the administration and with Congress.

Ronald Reagan made his economic goals very clear: lowering the rate of inflation, reducing the government's share of gross domestic product (GDP) while increasing defense spending, lowering tax rates, and reducing government regulation. Although he left it to others to work out the details, he made these things happen because of his skills in speaking to the American public and his ability to compromise in working with the Congress. He succeeded in achieving his goals, although never to the extent that he wanted. Government spending fell from 21.6 percent of GDP in 1981 to 20.5 percent in 1989, while the defense share rose from 5.0 percent to 5.5 percent, taxes fell from 19.1 percent of GDP to 17.8 percent, and the fiscal deficit excluding interest on the national debt (the primary balance) fell from 0.3 percent to minus 0.3 percent.

Although the Democrats had an overwhelming majority in the House of Representatives for the entire eight years of the Reagan presidency, the President achieved major tax reform (a revenue-neutral reduction of the top personal tax rate from 50 percent to 28 percent), a major reform of Social Security (raising the future age for full benefits from 65 to 67), and a free trade agreement with Canada.

The Federal Reserve under Chairman Paul Volcker (who had been appointed by President Jimmy Carter and later reappointed by President Reagan) achieved a rapid fall in inflation from 12.5 percent in 1980 to 3.8 percent in 1982 and 1983. This disinflation involved double-digit interest rates and a sharp economic downturn. One of my challenges as CEA chairman was to defend the Federal Reserve's actions against critics both inside and outside the administration.

The overall budget deficit increased sharply from 2.5 percent of GDP in 1981 to 5.9 percent of GDP in 1983. The 25-percent cut in personal tax rates that was enacted in 1981 was not expected to result in such a large deficit increase because, with tax brackets not indexed to inflation before 1986, it was projected that the high inflation that prevailed before the tax cuts would raise taxable incomes to offset the cut in tax rates. The unexpectedly rapid fall in inflation reduced the offsetting tax revenue. Although some of the rise in the fiscal deficit was also due to the recession that began in 1981, a net increase in the structural deficit remained. I joined forces with Budget Director David Stockman to argue that revenue increases as well as spending cuts were needed to shrink that structural deficit. Although the political side of the White House criticized me for this position, President Reagan made no objections and did support annual revenue-raising changes in corporate taxation while sticking with his promise not to raise taxes on "hard-working families struggling to make ends meet."

Although there were very good economists in several different cabinet departments, I realized that they each had two roles. In addition to advising the cabinet member who was the head of their department, they had to represent their department's position at interdepartmental meetings. I therefore found myself debating with these economists at meetings while suspecting that they were presenting their department's positions rather than their professional judgments. Perhaps they didn't mind losing some of those debates.

In my meetings with economic officials of other countries, I came to appreciate the unique role of the Council. As CEA chairman, I reported directly to the President and presented my own views in testimony to Congress. In contrast, the senior economic officials in other countries were often political figures rather than professional economists, or were economists who reported only privately to a minister of finance.

The team at the CEA is also unusual in being academics serving for only one or two years (except for the very valuable long-term statistical staff). This meant having very high quality people who brought up-to-date professional thinking, but who had to learn quickly the details of policy issues. William Poole and William Niskanen were already members of the CEA when I arrived and continued to work with me during my two years. The people I recruited as members of the staff included Democrats as well as Republicans, chosen for their analytic abilities, including Larry Summers, Paul Krugman, John Cochrane and Jeff Frankel, as well as younger economists Ken Froot, Larry Lindsey, Greg Mankiw and Katherine Utgoff, and others whose political affiliations I did not know. Although the White House personnel office was surprised when they eventually discovered some of their political affiliations, there was no attempt to change these appointments or limit what I did in my second-year appointments.

One of the many pleasures in working with President Reagan was his positive and optimistic attitude. It no doubt made it possible for him to work successfully with both Republicans and Democrats in Congress. But it sometimes made it difficult for me to convince him of the need to adopt certain policy changes. I recall one occasion after I had just had one of my Oval Office meetings with the President in which I said that it would be very risky not to make a particular policy change. The President asked whether continuing with the current policy was sure to create a problem. I said that I couldn't be certain of that but that the current policy would have a very low probability of success. I thought that my argument would have persuaded a typical prudent corporate CEO to make the change that I was suggesting. But the President decided not to do so.

As I left the Oval Office I realized that the President's optimism and his willingness to take a long shot on policy was not an accident but was based on his own life history. He started as a radio sports announcer but was soon a major movie star in Hollywood. When his movie career came to an end, he eventually went on to become a popular California governor. He later ran for the nomination as Republican candidate for the presidency but was defeated. But the next time around he won the nomination, was elected overwhelmingly, and was reelected four years later with an even larger margin. And there I was, after his long string of improbable successes, trying to persuade him not to do something because it was unlikely to happen.

and policy analysts throughout the Federal Government often hold similar views as CEA, but CEA is unusual in that providing an economic perspective is essentially its sole institutional purpose (see Box 7-6 for former CEA Chairman Martin Feldstein's discussion of CEA's unusual institutional structure and CEA's role in informing fiscal policy during the Reagan Administration).

CEA's academic character also helps to bring fresh perspectives on policy into the government, both by bringing in new people who have new ideas, and through keeping open the channels of communication with academia. It also means that CEA's views about policy tend to reflect economists' current understanding of how best to promote the public interest. For example, Charles Schultze notes that CEA regularly supported antitrust policies under the Eisenhower, Kennedy, Ford, and Nixon Administrations, but that its support for such policies waned during the 1980s as the economics profession's views shifted (1996). In recent years, growing evidence of "economic rents" has led CEA, along with many in the economics profession, to increasingly emphasize the importance of fostering more competitive markets as a means to address inequality and raise real incomes (see discussion in Chapter 1). In this way, Edwin Nourse's view of CEA as a "doorway through which the best thinking of systematic economics … may be brought into clear and effective focus at the point of executive decision as to national economic policy and action" has been vindicated (Norton 1977).

Of course, relying on short-term academic economists also presents some notable challenges: CEA's staff have little institutional memory and often do not enter government with much knowledge about policy decision-making processes or much understanding of the details of how Federal programs function. In addition, as discussed above, though it is critical to provide unvarnished economic advice, such advice is likely to be more useful if it is at least presented with an awareness of the broader political context. These constraints result in a substantial learning curve for many incoming CEA staff, and if they are not surmounted, can present barriers to engaging effectively in the policy process. Some CEAs have attempted to attenuate these obstacles by including a few government economists on staff and by relying on several career staff members for institutional memory.

Conclusion

Many of CEA's contributions are due to its unique institutional structure: that it is a small organization with no regulatory authority of its own, few direct operational responsibilities, and populated by academic economists. Yet its contributions are also dependent on the ability of its staff to balance operating effectively in a necessarily political environment without being overly influenced by politics, and to be effective in advocating for their positions while providing objective economic advice. All in all, given the divergent objectives reflected in the Employment Act of 1946, CEA's turbulent early years, and its unusual institutional structure, CEA has proven to be a durable and effective advocate for the public interest.