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Remarks of Timothy F. Geithner: A Conversation  
with the U.S. Treasury Secretary

Lunch Annual 2009

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## Remarks of Timothy F. Geithner: A Conversation with the U.S. Treasury Secretary - Lunch Annual 2009

[START TAPE ROSE GEITHNER]

MR. CHARLIE ROSE: With a special honor to have the Secretary of the Treasury here. I want to--you know his background and his biography, and New York Fed, and working at the Treasury. I guess you take he and Ben Bernanke have no one, no two people have been at the center of what we've been going through more than the two of them.

We want to talk about that today and where is the recovery and what are the challenges ahead. Some of the things we talked with Tim - - with Jamie Diamond about. But I want to being with this note. Everybody talks about our Secretary of the Treasury in terms of how young he looks. And I think it was Pete Peterson who famously said I didn't know that the Secretary of the Treasury was only 12.

MR. TIMOTHY GEITHNER: I'm getting older.

MR. ROSE: That's what I was going to say. Has this job aged you at all?

MR. GEITHNER: No, I'm getting older.

MR. ROSE: All right. Let's assume there's a big desk in the Treasury Department and you sit behind it, and there is a box that says long range. And there's a box that says intermediate. There is a box that says urgent. What's in the urgent box?

MR. GEITHNER: Urgent is to get the economy growing again, growth led by private demand, private investment; bring unemployment down so people who want a job can have a job. Urgent is laying the foundation for better education, better public infrastructure, healthcare reform, make people more confident we're going to get this government doing things governments have to do.

Governments have to do better if we're going to productive grow substantially in the future. And urgent is to fix this financial system, this still broken financial system, terribly broken regulatory framework we have that was the cause of the crisis and fixing that with the reform is going to be an important part of restoring some basic sense of

confidence in the financial system as a whole.

MR. ROSE: What do you think you've accomplished and how fragile is that accomplishment?

MR. GEITHNER: The most important thing that you can say we've achieved so far is to bring an economy that was basically at the edge of catastrophic collapse and depression back from the brink to restore some basic foundation of stability, and to bring about the early signs of recovery, just the early signs of recovery. And that's the necessary thing.

It's necessary for any--nothing is possible without having achieved that. And that is something that if you look back at history governments normally have taken a much longer time to do. And I think we achieve that initial stability, initial signs of recovery much more quickly than I think many of us expected, and much more quickly this happened in past crisis.

MR. ROSE: Two prongs of this obviously have been the stimulus and the financial sector. Let me talk about stimulus first. Everybody's asking the question what can you specifically say the stimulus, the \$787 billion stimulus plan has accomplished and do we need another one?

MR. GEITHNER: Stimulus was the recovery act combined with what we did to make people believe we were going to hold the financial system, make sure it had enough capital, make sure you get a credit flowing again.

Those two things were enormously important in helping bring business and consumer confidence back from the bottom, helping arrest an economy that was in freefall globally.

And if you look at when things started to turn in terms of equity markets, broad measures of confidence, and ultimately in growth, the turn came when people saw the - - passed here, governments around the world moving to do the same kind of thing to put a fair amount of financial force into the economy to compensate for the collapse and private demand of collapse in confidence.

So those achievements you see today in terms of - - , are the consequence of policy, of governments doing what governments--only governments can do in a financial crisis. And you couldn't have done it just with financial sector force and you couldn't have done it just with recovery act

tax cuts and expenditures alone.

You needed both working together along side what central banks were doing around the world.

MR. ROSE: How do you measure the health of the financial sector today?

MR. GEITHNER: The financial sector today is in a much stronger position than it was, but it's a mixed picture. Major financial decisions have much more capital today and a much stronger position to withstand the realistic view of pressures ahead.

Small banks, some regional banks still face a much more challenging environment. Mortgage market now is still very damaged, depends almost entirely on what the government is doing through the GSE, other government programs. There are parts of the economy businesses that are very hard time getting credit.

Small businesses are more dependent on banks, therefore more vulnerable if they were unlucky in the choice of bank, if they had a bank that was at the weaker end of the spectrum. They have fewer alternatives. So they're having a hard time getting credit.

But in general if you just step back, all broad measures of confidence in the financial system are substantially better. The price of credit has come down dramatically. It is significantly easier for most significant companies to borrow to raise capital to raise money, and those are really important things.

You know you can't have growth without credit. You won't have recovery unless you have--unless we diminish these financial headwinds that typically have caused recoveries to be weak in the past.

MR. ROSE: How important and what does it say I mean in terms of credit demand outside of major urban areas, that it hasn't begun to flow? Does that reflect the fact that small businesses have not yet had the confidence to buildup their inventory, their confidence to add employees, their confidence to get back to making a real contribution to the real economy?

MR. GEITHNER: Again, I think broadly you should say there's three

types of things happening and they all matter. One is the economy is coming out of a long period of time where large parts of the American economy borrowed too much and took on too much debt.

And that has to be inevitably followed by a period where people improve their strength in their balance sheet to save more. Second thing happening is what you referred to. Is that people face a lot of uncertainty about the strength and demand for their products, so they're borrowing less, they're more cautious.

They need to borrow less because demand has fallen, but they're more uncertain. That's about a recession, a deep recession. And the third thing is you're seeing the inevitable and exertable, tightening of credit standards after a period where they were too loose.

You know what happens is what's tragic amount these things are you have a long period of excessive loosening of credit standards. Everybody follows the market down. It gets way past the point of what would have been realistic and - - prudent.

And then when the recession comes, things tend to overcorrect. And the overcorrection itself creates a lot of risk. You have viable companies with good businesses starve for the kind of credit they need to expand and hire more people. And that's why financial crises can be so damaging.

And why they can make recessions much deeper, cause much more damage than they should. And that's why the basic lesson of these things is you have to be aggressive in trying to work against that. And that requires sustained efforts to get capital into the financial system, and try to make sure you're getting the engine of credit working again.

MR. ROSE: China, Chairman Bernanke has said and you have said that Asia is leading the recovery back. I mean they're talking about growth rates for 2009 of close to 8%. What are the implications of that for the United States?

MR. GEITHNER: They are largely good for the United States, and they will help improve the odds that we come out of this more quickly with stronger growth. Generally we are in a remarkable strong position to benefit from strength in those emerging markets.

Most of the large major global companies in the United States are very active in those markets and they benefit directly where demand there increases. And they're likely to lead this recovery. And so I would say on balances, it's good for the United States.

MR. ROSE: But will it change because they will export less? Have they created internal demand for their products that were coming to the United States and Europe?

MR. GEITHNER: That process is only beginning. But they all confronted a situation where having run economies based primarily on export demand. They saw what happened when that demand fell off the cliff.

And I think they recognize that as we're saving more as a country, that they're going to be able to rely less on demand of the United States, fueling exports there, and so they're going to have to shift source of demand to domestic demand to consumption. And that process is beginning.

I think they recognize the reality, you don't want to live through that again, don't want to be as vulnerable to them in the future. And so there, if you listen particularly to what the Chinese are saying and many countries in that region are saying, they're beginning that shift. But to be fair, it's going to take some time and it's only just beginning.

MR. ROSE: Okay. Do they--what questions they have for you at a G20 meeting in Pittsburgh say about our economy? They insist they're concerned about the American economy. They insist also they still have confidence.

MR. GEITHNER: I believe they do and I think if you look at the way the world views the United States today, if you get classic signs, you see a lot of confidence in this economy. A lot of confidence in our capacity as a country to lift ourselves out of this.

But their concerns are like the concerns of any American. They want to know like Americans want to know are we going to grow again. Is this financial system going to be more stable in the future?

They want to know whether we are as a country going to find the will to bring these fiscal deficits down over time as growth is established. Those are understandable concerns, but they're no different from concerns of any American and no

different from anybody who occupies my office would have.

MR. ROSE: Okay. Just a tangent, anybody who occupied my office. You have been at the center of this; first at New York Fed and now as Secretary of the Treasury. Tell us what you have learned. Tell us what it's been like at the center. Tell us what scared you. Tell us where you know where the worries are you have at this moment, that this is a sustainable recovery.

MR. GEITHNER: That's a long complicated question. We could talk about that for days, for hours. I think right now and this is not a challenge that is unique to the United States. Right now we face this very difficult balance.

We're trying to make sure again we're doing everything necessary to improve the odds that growth recovers, that we bring unemployment down, that private investment starts to be and people find that spark again that makes them more confident that they can take risks again.

And that's going to require further sustained support by policy, by government, and not just in the financial sector, but more generally. But for that to work, people have to also be confident that we're going to when we have growth established again that we're going to go back to living within our means.

MR. ROSE: Right.

MR. GEITHNER: And that is an enormous difficult balance. It's a balance that many countries throughout history have gotten wrong. The typical mistake is to do too little as the crisis intensifies and then put the brakes on too early. We did this in the 30s.

MR. ROSE: Right, right.

MR. GEITHNER: And I think that is the most important challenge most--and again, they're linked because growth will be weaker in the future, in the near term if people aren't confident that we're going to be able to address these long term and year term fiscal challenges.

And yet I think everybody understands right now that we're only at the earliest stage of recovery. And when you get growth back, if we're going to be able to begin to address those long term fiscal challenges. And that's the difficult

balance.

I think that's a difficult balance and I think people should understand that this President and I think he will have the support of Congress to do what it takes when we get to that point, but I think they also understand that the biggest imperative that we face now is the imperative of growth.

MR. ROSE: Okay. And that's what worries people because they look at some of the forecasts and they see we may only be experiencing in the near term certainly through 2010, perhaps later, moderate growth. And they look at the worry of a kind of sustained unemployment, not at 10%, but not coming back down to where it was before. How do you deal with that? How does the economy deal with that? How do you accelerate?

MR. GEITHNER: Well I think that you know you need to make sure again you have credit flowing. You make sure that you're creating incentives for people to start to invest again. And you need to give the economy a little bit of time to work its way out of these huge problems that help create this crisis.

That cannot happen--it's not like flipping a switch. It can't happen over night. But I think you should be encouraged by what you're seeing so far. You know Americans are saving again which is a healthy thing. We're borrowing much less from the rest of the world as a share of our economy than we were just three years ago, two years ago.

Our current account deficit which measures how much we borrow from the rest of the world is less than half its previous level. It's now below 3%. You are starting to see an economy that's growing and the strength of growth is broadening, and that's encouraging, too. So I think you're seeing some encouraging signs. We just make sure we're reinforcing that process.

MR. ROSE: Are we becoming or will we become an export economy?

MR. GEITHNER: We have always been a major export economy and the most successful companies in America are international companies. And if you look across the country across industries, small and large, small and medium companies, too, have a big stake in growth in the rest of the world. And that's one our--again, one of our great strengths.

That's because that we've had an economy that has created great incentives for innovation and you've had most American,

you have economies you know American economies across many industries still. They're at the frontier innovation. And that's going to be our great source of strength in the future.

MR. ROSE: But is there paradox here in that you need in terms of America's tradition of being a consuming country and the Asian countries being saving, and you need for them to spend more and you need for us to save more, but at the same time, we need a stimulus for people to buy things to create jobs and to create companies that will be expanding. Is there a paradox, and a push and pull on that?

MR. GEITHNER: There is I think, but again, I think if you look at what's happening so far, you should be encouraged by the initial signs of the adjustment. Again you see more rapid growth in many parts of the emerging world. That growth is gradually shifting to domestic sources. It's less export dependent. We're saving more as a country.

And that shift is a necessary shift. It's going to take some time, but I think it will happen. And it will, if we get it right, growth will be stronger, more sustainable, more balanced here. You'll have economies everywhere less prone to crises. But we're just at the beginning of that transition, - - .

MR. ROSE: The deficit, are we going to need another stimulus plan do you think or not?

MR. GEITHNER: The Congress is now looking at a range of choices about whether we should extend unemployment benefits, a variety of other targeted tax programs, things like that. There's going to be a good case for extending many of those. That will provide some additional near term support for the economy. The recovery act itself, though, was designed to provide a pretty substantial amount of support for I think a two year period of time. And about half of that effect is still ahead of us.

MR. ROSE: Really, a half? Because Christian Roman said most of it will come in 2009.

MR. GEITHNER: Well you're at the point where the investments in public infrastructure which are more employment intensive than many other things, those things are structured so that a bunch of that comes--is still ahead of us. But the overall

package was designed so it's a two year program and it provides sustained support of that two year - - . So you have a bunch of that ahead of us still, and I don't think we're in a position yet where we need to make a judgment about whether we need to think about substantial additional incremental stimulus.

MR. ROSE: So that decision hasn't been made?

MR. GEITHNER: And does not need to be made yet.

MR. ROSE: Does not need to be made.

MR. GEITHNER: Yeah.

MR. ROSE: Give us a sense of how you look at the deficit and how does this government look at the deficit because wherever I go, it always arises as a huge concern on the part of people in an audience.

MR. GEITHNER: Look it's--I think it's just it's better to say it's starkly. When you start as we did this year with the crises intense, a recession this deep, you know this incredibly damaging loss of confidence, the only choice you have if you want to solve that problem is to try to create incentives for people to spend and use the government to take risks the private sector cannot create.

And that is expensive in the near term. If you don't do that, though, you'll make the long term challenges much worse because growth will be weaker. You see much more damage to your revenue base; future deficits will be much higher.

So the conservative prudent necessary step if you're fiscal hawk or not in a crisis like this is you have to have the government go in and do only what governments can do. But it has to be designed to be temporary.

You have to make incredible you will withdraw that when you have growth established. Now we have two types of fiscal problems going out. We have a very long term fiscal problem which is driven primarily by what you've seen happen in terms of the rate of growth and healthcare costs.

MR. ROSE: Right.

MR. GEITHNER: And you have a deficit problem that is more about the medium term. Both are unsustainable. The best path towards fixing our long term fiscal problem which are the

most daunting ones, has to go through healthcare reform, that brings down the rate of growth and costs. So we are already coming, we're coming quite close to having in place comprehensive healthcare reform that will reduce the growth and long term healthcare costs, and help make a huge improvement in those long term deficits.

MR. ROSE: But it will still be a trillion dollars over ten years.

MR. GEITHNER: No, but it will be paid for within that ten year window. Not add to the deficit in that ten year window, and more importantly it will help bring down our future deficits driven by healthcare costs. So we are now even in the midst of this recession starting to do the things that will be necessary to deal with those long term deficits.

Now on the medium term deficits, again when growth is underway and we're confident it's sustainable, then we have to bring those fiscal deficits down to a sustainable level. And that's going to require difficult choices. We have work with the Congress on that.

We have to make sure that Congress makes credible it's commitment to do that. And they're slightly different challenges, but I think that you're seeing now again encouraging signs of what will be important steps to improve our long term fiscal health.

MR. ROSE: Regulation and regulatory reform. What do you think is necessary?

MR. GEITHNER: Two key things; easy to say, hard to get right. You need a much stronger set of protections for consumers and investors. You know we saw just a colossal loss of confidence in the basic integrity of the system. The protections the government has to provide in this area, and we need to fix that.

Second is to do things to make the system more stable in the future, less vulnerable to crises. And that requires creating a system in which you have more effective constraints and risk taking through required restrictions on leverage for capital requirements.

And it requires you have a system that's strong enough to let people fail. You can let people fail without causing enormous damage to the system as a whole. And that requires giving the government better tools to manage those failures

with less cost to the taxpayer, less collateral damage to the American people. Those are the key things.

Consumer investor protection and a more stable system with less morale hazard, and better market discipline, and less risk of catastrophic failure.

MR. ROSE: There'll still be companies too big to fail.

MR. GEITHNER: Let me say it a little bit different. You want to build a system where neither investors nor institutions live with the expectation that the government will come in and insulate them from the cost of their mistakes in the future. And to make that credible again you need just two things.

And again these again they're hard to do, but they're critically important. You need to make the system strong enough that it could withstand the effect of a large institution failing.

You need to make sure they're living with strong enough shock absorbers, capital cushions, that they can withstand the effects and the trauma that comes if one of them manages themselves to the edge of the abyss.

We need to give the government the capacity and we did not have this coming into last year, and it was a tragic failure. You've got to give the government the capacity to manage the disillusion, the unwinding of those firms. Not just save them from the - - or failures.

Not to give them the chance of redemption. Not to make it possible for them to survive again, but to make sure that they are unwound with less burden on the taxpayer and less risk of trauma to the system as a whole.

MR. ROSE: What have you learned in what you have done so far in terms of rescuing American companies?

MR. GEITHNER: In what sense, Charlie?

MR. ROSE: Well I mean for example what is the lesson of you just suggested that you need to have a system that you have in place to deal with--

MR. GEITHNER: [Interposing] Not to rescue, but I would think of it this way. The ideal system is a system in which if an individual firm manages itself to a point that they cannot survive on their own, that they fail. And you want to make

sure the rest of the system, viable institutions, are not so damaged by that failure that they can't survive on their own, too.

So you want to put a firebreak around that institution and make sure the fire can't jump the break, and imperil the viability of viable institutions. That's the system you have to design.

MR. ROSE: And how do you do that, that's the question? How do you design that firewall?

MR. GEITHNER: You need to make sure that people outside are strong enough, they have a lot of capital against the remote low probability risk of a big shock like we went through, and you need to make sure the government can step in earlier with better tools to manage the failure of that institution that you--you know you just don't want to protect from their failures.

MR. ROSE: How long will the United States Government own such a large portion of AIG and such a large portion of Citicorp?

MR. GEITHNER: Not a day longer than we need, too, and I don't think that long actually.

MR. ROSE: Really?

MR. GEITHNER: Yeah. I think we're in a position now where you've already had substantial amounts of capital come back from banks to the treasury with interest to the taxpayer, reasonable return to the taxpayer frankly. And I expect you're going to see a lot of the rest of the money out there and the system come back relatively quickly as well.

And that's something obviously we want to encourage because you know private capital is better than public capital. Better for a bank to have private capital rather than government capital. And we would like nothing better.

MR. ROSE: Are we talking about a year, two years, three years, ten years?

MR. GEITHNER: It will differ depending on the institution, but I think for the major banks in the country, for the vast bulk of banks in the country, I think that money will come back relatively quickly. Now I inherited a formidable set of problems in our economy and there are other parts of the

system where we were forced to act.

We acted with great reluctance. But we did it because we thought the alternatives would be much worse for the American economy, and some of those are going to take a little longer to unwind to come back.

MR. ROSE: What are you talking about when you suggest that?

MR. GEITHNER: I would say for example in the automobile industry.

MR. ROSE: Right.

MR. GEITHNER: Although we've seen very substantial restructurings put in place that were designed to allow these institutions to be profitable without government support. Even the event you have a very prolong slowdown in auto sales or slow recovery in auto sales realistically it's going to take some time for the government to gather those companies.

We'd like to be able to get out as quickly as possible and we've been very careful, Charlie, to design our framework so that we are not in those companies involved in day to day management decisions. We're not going to get involved in things except those that are hugely materials protecting the taxpayer's interest.

And we want and we think it's - - to the taxpayer and the interest of the companies for us to get out as quickly as we can.

MR. ROSE: But is there an exit strategy?

MR. GEITHNER: Oh yeah absolutely.

MR. ROSE: Just to use the words that Chairman Bernanke uses.

MR. GEITHNER: Yeah and you can see the signs of it already as I said. We have already shutdown a number of the emergency programs that were put in place to arrest the panic; money market guarantee fund closed.

A huge number of the special facilities that I helped design when I was at the New York Fed have been shutdown or you've seen demand fall to trivial levels now. So you're seeing us gradually emerge from that. As I said, banks have already repaid \$70 billion or so on capital to the Treasury already.

You expect to see a bunch back. So we're beginning that

process already of changing from the emergency things to things that are going to be necessary to sustain for example to help get small business credit flowing again.

MR. ROSE: Now did the stress test cause some banks who were planning on paying back their tart money to have to slow it down because they had to go meet the capital needs determined by the stress test?

MR. GEITHNER: No, the stress test did an enormously important thing. When we came in again if you look back at the beginning of this year, banks could not raise capital. They were reducing their balance sheets, cutting back on lending; starving the economy of the oxygen it needs to grow.

And that was in part because there was such a cloud of uncertainty about what the scale of losses they faced was going to be in the event we had a more prolonged recession.

So what the stress test did is forced these institutions to disclose a remarkable amount of information about the quality of assets on their balance sheets, the losses they may bear in that context, and that allowed the market to differentiate among them to make judgments on their own about how much risk these firms faced.

And that made it possible for them to go out and raise private capital. And you saw substantial amounts of private capital come into the financial system. But by going through this process of transparency and disclosure by lifting the hood, letting everybody else look in under the hood, we allowed--made it possible for a huge amount of capital to come into the financial system from the private sector, not from the government.

In fact, I don't know if you know this, Charlie, but I've written no checks to a major bank since I came into office into this job in part because we were able to adopt a strategy that made it possible for that recapitalization to come from the private markets, not from the taxpayer.

MR. ROSE: Uh-huh. Has all the tart money been spent?

MR. GEITHNER: What the tart money--you mean in terms of the broad authority - - ?

MR. ROSE: Yeah, right.

MR. GEITHNER: No. We are using that authority very carefully. As I said, because we're winding down the emergency authority, we are going to probably be able to reduce significantly the amount of money we borrow to finance this recovery in the financial sector.

It's probably going to cost the taxpayer a substantial--a small fraction of what we estimated early part of this year. But, Charlie, you know again I want to emphasize, this process of repair is still underway.

There are large parts of the economy that are still financial system is still damaged, parts of the economy still starved of credit, and we want to make sure that we are reinforcing that process of repair not prematurely in the end.

MR. ROSE: What could derail the best plans you have? I mean what is out there, what would be a landmine that could put us back in the hole?

MR. GEITHNER: You know I think everyone's got their list of challenge and risk, and I think they're the obvious ones. And in some ways it's a good thing people are so focused on this or worried about them because that means people have built in some expectation that there's some probably those things will happen.

But I think you know this, Charlie. What surprises you is the things you didn't anticipate. What can hurt you is the thing that where there was a failure of imagination, the things that are just hard to think--

MR. ROSE: [Interposing] What has surprised you?

MR. GEITHNER: Many things have surprised me. It would be a long list I'd say.

MR. ROSE: Well what's at the top of the list?

MR. GEITHNER: Again I would say a principle lesson of this crisis is that we had a long period where people just tended to give too little weight to the improbable event that could cause catastrophic damage.

And I think the basic lesson of what you saw in terms of how much consumers borrowed, how much banks lent, how much risk investors took, what expectations were about housing prices or growth. You saw people because you had a long period of

stability project that stability in the future.

And that of course bread instability and the basic lesson is that people tend to give too little weight to the catastrophic risk. And the best solution to that is to make sure that the system is run more conservatively with more shock absorbers against the unknown.

MR. ROSE: Yep, meaning that people didn't believe it was as bad as it was?

MR. GEITHNER: No, I'm thinking about on the way up.

MR. ROSE: Okay.

MR. GEITHNER: On the way up - - . When things turn, it goes the other way and you see people becoming you know you saw economic activity just stop, credit stopped flowing. You saw a huge rise in fear and uncertainty, and that's the point when there's no solution except for the government to step in and fix the problem.

MR. ROSE: Yeah. I remember seeing you in May of 2008. And I said to you at that time what's the most surprising thing about what we were going through. This was after Bear Stearns before Lehman. And you said to me how fragile things are.

MR. GEITHNER: Yeah. I think we built a system that was exceptionally fragile, tragically fragile.

MR. ROSE: Yeah.

MR. GEITHNER: And you know the way these things work, the consequences of those failures aren't born solely by the people who made the mistakes. They caused just a huge amount of damage, indiscriminate damage to the banks that were conservatively run, the companies that were conservatively run, to families that were prudent, didn't borrow beyond their means.

The damage is indiscriminate and that's why sort of the just and the necessary thing to do in a crisis is to have the government commit to do what it takes to fix it.

MR. ROSE: Confidence. You've used that word a number of times and so has the President and so has the Chairman of the Fed. Give us a sense of what that's about. I mean what is it you see out there that people don't have confidence in? Is it

Wall Street? Is it the government? What is it that is at the core and what do you do to restore that confidence whether you're the government, a Wall Street firm, or a business in main street America?

MR. GEITHNER: Well I think you've had a prolonged sustained loss of confidence among Americans in a whole range of public institutions, magnified, accelerated, intensified by this crisis. You've seen a colossal loss of faith confidence in the financial system.

And you see huge uncertainty about what the future is going to mean, what this is going to mean for the future. And people--that is going to make people cautious and more uncertain for a time. But again I think you can start to see some encouraging signs of change there. You know we do measure a consumer investor confidence.

MR. ROSE: Right.

MR. GEITHNER: And those numbers are still--they still reflect a fair amount of uncertainty. But they're substantially up off their bottom. And if you look at how firms are behaving now, how consumers are behaving, they're starting to behave in a way in which they're starting to exhibit a little more confidence about the future.

But you know we need to do as--we need to work very hard and this requires the Congress, too, to demonstrate that we can make governments do better what governments have to do. And you know we have an economy that's going to depend always on the market, but market can't solve all problems.

And markets will not work well as we've seen unless it's done in the context where there's a sensible framework of regulation over the financial system where we're graduating people from high school and college that have the skills they need to compete in this world.

We're fixing in a sense probably how people use healthcare, - healthcare. I mean we don't just have a typical recession of somewhat greater intensity than normal. We came into this period, Charlie, with you know a long sustained rise in equality, a substantial erosion in the relative quality of U.S. education.

If you're born poor in America today, the chance you're going to get a quality education is much lower than the change if

you're born fortunate. Same is true for healthcare. We're incredibly wasteful in how we use energy in this country. We've had sustained erosion in basic quality of public infrastructure. And those are things we have to fix.

And I think part of confidence is demonstrating that we have the will and the ability to do those things better over time.

MR. ROSE: But that's the big question. Can you do that without increasing the deficit beyond manageable means to a threatening level?

MR. GEITHNER: I think we can. I think a lot of that is about doing things better. Some of it cost money, but we're being very careful to make sure for things that cost money, we're going to pay for them over time.

We can't afford to do what we did too often in the past which to make very large commitments to cut people's taxes or to finance huge expense of - - without paying for them. And demonstrating we're able to do that is important. You need to build back that confidence carefully step by step that we can make this government do a better job of things only governments can do.

MR. ROSE: Explain to us the regulatory battle that's taking place now because we heard Administration spokespeople going out a couple of weeks ago saying that people in the business world who've received helped from taxpayers and had gotten their business back on track to speak, sort of were back in same ole same ole, and they were down in Washington lobbying against reform that they thought was necessary and that you think is necessary.

MR. GEITHNER: Well it's what happens, it's the way the system has worked. And it's partly why we had a system so fragile because we allowed--

MR. ROSE: [Interposing] Because there was not enough enforcement of regulation or not enough regulation or too much lobbying against regulation with teeth?

MR. GEITHNER: You know we had a--how should I say it, a crazy system, screwed up system. You have parts of the system that had a lot of regulation. You have parts of the system with very little regulation. You allowed risk to migrate where there's little regulation.

You let a system where an institution could in effect choose their regulator and they could structure a particular transaction in a way that would minimize the tax or regulatory capital consequences. And that created a more fragile system.

That system was the consequence of choices made by Congress and by regulators over time in response to effective efforts by the financial community to design a system it thought would be in its interest. It was not in their interest, in the interest of the industry to run a system like this.

This huge imbalance in the quality scope of regulation meant that you had well run conservative institutions losing business to firms doing the same thing; writing mortgages, writing credit to business, doing the same basic economic function with lower capital requirements or nobody looking at them. And that is not good for a financial system.

And to allow that degree of competition in - - standards - - caused a lot of damage. It does damage to well run institutions. So I think that the financial industry of the United States has a big interest in helping work towards a well designed set of reforms that fix those basic problems.

Now we want to get this right. We want to do it carefully. It's normally the complex thing to do and I think we've got a very good chance, Charlie, of getting this right and having a very strong package of reforms passed.

MR. ROSE: Okay, but tell us what right is, too?

MR. GEITHNER: Well again, right means a better balance between innovation and stability, between inefficiency and resilience, between allowing competition to provide innovation for consumers investors without the risk that you leave people terribly vulnerable fraud and epulation predation [phonetic].

And without a system that is as vulnerable as ours as been to periodic crisis. You know we had a system where every four years or so we had a pretty significant financial storm. Nothing like what we went through this past year, but pretty significant financial storm and we should not have a system that is that fragile.

And getting that balance, we got that balance wrong. And we got to make sure we get it better and it's going to be

significantly about getting regulation better design, but something that's going to be about more regulation.

MR. ROSE: Okay, but is there going to be a battle in Washington between those people who believe that the system has a crisis of confidence, and those people who believe that more regulation is not in the interest of themselves or even of the economy?

MR. GEITHNER: But there are some parts of the financial that I'm sure believe that the system worked fine and the regulation was well designed. But there's not really many of them that take that view. And my own sense is that the best run institutions in the country believe they have a strong interest in a strong package of reforms.

Now they're not going to agree on the full range of things that will become law or that we're going to help become law. And you wouldn't expect them to agree on them. But I believe that you know the financial system of the United States still has these remarkably important strength.

You know we are still I think the best country in the world at taking the savings of an American and maxing them to the idea if somebody wants to grow a company. We're just terrifically good at that and we're going to make sure we sustain that advantage.

And I think that are role in the global financial system, the power of this city in the global economy, global finance of the center of the American finance will be stronger, our role better established if we do the kind of reform changes that are going to make people more confident investing here in the future.

MR. ROSE: Uh-huh.

MR. GEITHNER: So again I think there's a strong interest in the financial industry in reform. And of course you're going to see people fight to preserve what they think is in their short term economic interest, and we can't let that undermine--

MR. ROSE: [Interposing] And what should be done publicly on exchanges and the like.

MR. GEITHNER: Well I think derivatives is a very good example. You know what we're proposing is to bring the derivatives

market onto central clearing.

MR. ROSE: Yes.

MR. GEITHNER: So the risk can be more carefully managed, more clear, less risk of contagion in the crisis so that you can better police for automanipulation. If there's more transparency not to markets and deregulators, those are sensible necessary changes. And again, I think there will be broad support for those reforms across the American economy as a whole and in Congress.

MR. ROSE: When this crisis began, people like me were always asking these sort of philosophical questions like is this going to change capitalism. Is this changing capitalism?

MR. GEITHNER: You know I think it's changing fundamentally how people think about how they save, how much they save. And I think it is changing fundamentally how people look at risk. And I think those are going to be important things.

MR. ROSE: They're going to save more and they'll be more careful about risk.

MR. GEITHNER: I think they will think about risk as they should and this is what crises do is they make you give greater weight to what seemed an improbable event that can cause a huge amount of damage. Those things are healthy things. But I think, Charlie, I think the best answer to your question is it depends really on how good a job we do at fixing through financial reform the basic incentives in which the financial system operates.

MR. ROSE: And what will be the test for that? An economic growth rate? Stability of institutions?

MR. GEITHNER: Yeah I think that if you wanted to look back, what you want to look back over and you want to see a period of time where growth was more stable over a longer period of time rather than having periods where you know again everybody said every three years or so you have a classic pattern of real estate boom, credit explodes, other asset price rise, and the other side of that caused a lot of damage.

MR. ROSE: Speaking of real estate boom, where is the housing market and divide it into using \$500,000. I mean there was a huge housing inventory. Is that being drawn down?

MR. GEITHNER: It is. It's coming down. I think that you've seen now over the last three months or so little sign of stability in prices. Inventory is coming down, demand increasing a little bit. And those are encouraging signs.

You still have a housing market that is you know it's going to take a while to have that inventory run off and that process will take some time. But again, I think encouraging.

This was a crisis in which housing made the crisis worse, intensified the crisis in the early stages, but now you are seeing housing starting to stabilize and the continued weakness in housing is more a reflection of the fact that unemployment is still quite high and growth is still sort of it's still at it's early stages.

So instead of driving a recession now, it's more the weakness you see out there still just a more like a reflection of the fact that we're still coming out of this crisis. But initial signs of stability very encouraging largely because again of what we did to help bring interest rates, mortgage interest rates down and help provide a little foundation for recovery in a broader economy.

MR. ROSE: And recently the dollar has been weak especially against at Euro. What's the future of the dollar and 20 years from now we'll be looking at the dollar as a reserve currency of the world?

MR. GEITHNER: Absolutely. I think the dollar will remain the principle reserve currency for a long period of time. Its important Americans understand, though, that that role in the system is not a privilege. It comes with responsibilities and obligations.

It puts a greater burden on us to make sure we're doing things that improve the world's confidence in our capacity to run our economy carefully and prudently, bring our fiscal position down over time. Those are important things for people to understand.

MR. ROSE: When you go to China, what are the conversations over there about currency because you're not happy with the artificial way they manage their currency?

MR. GEITHNER: Well China's going through a very important transition. But let me try to put it in their words. I think they recognize and they've said this over time that

they want to move to a more flexible exchange rate system. That's important for them because it gives them the ability to set monetary policy to conditions in China, not import our monetary policy. That's important.

It also would be important to help them shift towards higher value added and more productive types of economy activities in the future. It will help facilitate this shift towards a more domestic demand, more sustainable growth in the future. And that's why they've laid out that basic path. So that's the conversation is they normally describe how they're trying to balance the challenges on that path.

MR. ROSE: Everybody talked about a new world economic order. How does it look to the American sector of the Treasury?

MR. GEITHNER: Well you know people mean different things about order. I think one thing you're seeing we're doing a lot to try to shape this is try to transform how we kind of front the big economic questions of our time by bringing the major economies in the world around a table together. You saw that in the G20.

MR. ROSE: Right.

MR. GEITHNER: So for the first time, rather than having the U.S. just talk to Europe and Japan, we're recognizing the basic reality that we can't solve these problems unless we have at the table countries like India, like Brazil or like China, and by giving them a seat at that table.

And by helping them understand the responsibility we all have to help build a system that's going to work, provide growth in the future, I think we have a better chance of working through these things more effectively in the future, and not being as late as governments were this time, and confronting the causes of the crisis, and acting to help address it.

MR. ROSE: You would argue that it's better for the United States to have a larger part, a lesser share of a bigger pie than a larger share of a smaller pie?

MR. GEITHNER: Our share you know we're still if you just take the institutions that were setup after World War II, - - Institutions, the - - and World Bank, in those institutions, we're you know roughly 18% of the votes. We provide about a quarter of the financial resources.

And that is roughly in proportion to our stake, our share of growth and economic output in the world today. So our position is not anonymously high today out of whack. The big disparity is that emerging markets as a whole have a weight in the institution much lower scaled. And that's partly because it's just taken a long time for the world to adjust and reallocate votes from the parts of the world that used to be much larger in relative size to those that are much larger today. And that's mostly about Europe.

MR. ROSE: How would you assess the level of global cooperation?

MR. GEITHNER: I would say that it was remarkable in the moment of crisis and we hope to sustain that cooperation as we deal with the reform challenges.

MR. ROSE: Okay.

MR. GEITHNER: Because you know the challenge of course is that you don't want that incentive to cooperate to fade as the crisis recedes.

MR. ROSE: And before the crisis, everybody said there's a fear of decoupling. It turned out during the crisis there was no decoupling.

MR. GEITHNER: Not at all. You had--

MR. ROSE: [Interposing] But you now have Asia leading the recovery and you're asking is there decoupling taking place.

MR. GEITHNER: I don't think there--again, I think that we've got an incredibly integrated world. I never believed the decoupling story. And you saw the world move together as confidence collapsed, economic activity collapsed, trade collapsed.

But we're obviously going to come out of this at different speeds. The U.S. came into this earlier than many countries. We've had a lot of very wrenching traumatic adjustment already happened to this economy. And I think we're in a better position because of that in some ways to emerge stronger, ahead of many of the major economies.

MR. ROSE: You mentioned the auto industry. What's going to happen or how do you see that unfolding?

MR. GEITHNER: Well of course ultimately, Charlie, what matters is you need to make products want to buy.

MR. ROSE: So that was the problem with the auto industry. Or was it their healthcare? They were really healthcare companies. Which was it?

MR. GEITHNER: It was a complicated mix of choices and luck. But you know governments can't solve that problem. Ultimately what determines the fate of companies is again whether they can make things that have value, people want to buy.

MR. ROSE: But now the government has a much more influential role in that than it has before.

MR. GEITHNER: No, we're not going--we cannot be in the business of helping them make those choices. That is not something this government can do. And we have been very careful as I said to say we are not going to be in the business of making choices about how they run these companies, make the next generation of cars. That's something these companies have to do.

MR. ROSE: So President Obama is not the CEO of General Motors.

MR. GEITHNER: I don't think he has any desire to be the CEO of General Motors.

MR. ROSE: Yeah.

MR. GEITHNER: I'm sure he doesn't.

MR. ROSE: When you look at securitization and the kinds of securitization that are being created, what will change in the future about the notion of what securities are being created on Wall Street? And if we get through this crisis, are we going to be back in the same place we were?

MR. GEITHNER: You know I think it's likely that they're going to be at least for a time more simple, easier to understand, easier for people to assess what the risk is in holding them just because there's been such colossal loss of faith in the things people used to rely on to make those judgments like federal agencies or their past models for what the models told you about the future.

But ultimately if there's an economic demand for a particular type of way to hedge an investment or invest risk, the market is likely to meet that demand. And what the job of government is to make sure is that there's enough capital held against those risks and so that you know we're not going

to run a system where we demand on people in Washington to peer into the future and decide that that particular type of instrument is inappropriate for people to hold or invest or hedge against.

We need to make sure that the system allows for that innovation or that risk of bringing the system down to the edge of collapse. And that just requires people to hold more capital against the risk they take and more capital against the inherent uncertainty we all live with in measuring those risks.

But I think securitization markets will--there's going to be an important role in our country for securitization markets. One way to think about it is this is in our system we rely on banks to provide about half the amount of credit. The rest comes through capital markets including through securitization. And that is generally a source of strength.

And if you look what's happening right now for example, credit by banks on balances falling mostly offset now by the amount of new issuance of securities. So you can have--you want to have a system where you have both a robust capital market people have confidence and strong banks so that a weakness in one--a strength in one can offset a weakness in the other.

MR. ROSE: What level of cooperation when you go to China or when you go around the world, what level of cooperation exists today in terms of those issues that are clear of the future? I'm thinking of climate change and those kinds of things. What kind of receptivity do you get when you go around the world?

MR. GEITHNER: You know my own sense, Charlie, you see a very broad consensus on this set of acute challenges we face from climate change to financial reform to trade poverty development. You know what's hard is translating that consensus into things that people prepare to act on.

MR. ROSE: Because they have their own growth dynamic.

MR. GEITHNER: Of course. And people have different views about the tradeoffs in that case. But you know ultimately I think the approach I think that we have to bring as a country to this is that it has to start by demonstrating to countries around the world that we're going to take care of our

problems.

That we're going to do things in this country that are necessary to put our own house in order. To demonstrate, we're prepared to do our part for those things. That's essential. Nothing is possible cooperation globally without that. People have to have confidence.

We need to be credible with them. Second thing that really matters is we have to come to the table with good ideas that will command consensus that people can follow. And where we can do those things, we can have enormous impact on not just the agenda, but how much progress we make together in achieving that agenda.

But it has to start with choices we're prepared to make here. You're not going to solve these things if you try to put the burden on others to do things we cannot do.

MR. ROSE: What's the economic future of Europe?

MR. GEITHNER: It's for them to--it's for them to shape. And I think that they've got a different mix of challenges than we do. You know you can in many ways look at what they've been through this and view it with some envy because they've had a much less pronounced fall in employment, much less pronounced rise on employment even though growth is very, very weak there.

And they've allowed--they run a system that gives much greater rate to stability than we have as a country. On the other hand, they have a very formidable mix of long term fiscal challenges. Their financial - - was significant, too, and they've got some hard choices to make in that context.

But Europe is roughly as large as us in economy. And we will be stronger, U.S. will be stronger if they come out of this crisis as quickly as possible.

MR. ROSE: I haven't talked about commodity prices. Oil is up over \$80 a share now. How do you see commodities?

MR. GEITHNER: Charlie, you know I generally don't talk about markets, but I would say this. I think the most important thing you've seen and this is an encouraging thing, what you've seen is - - contrast to what people--the way we were behaving early in this year, the first quarter of this year, last quarter of last year is you've seen people start to take

risk again.

You've seen them start to move out of the risk free asset. You start to then build in some expectation that global growth is going to recover. So I think most of what you've seen in commodity markets elsewhere just reflects that shift from acute concern amount a global depression or about a prolonged period of deflation, financial collapse to greater confidence, that there's a bit of a foundation to this and you're starting to see growth come back.

MR. ROSE: Latin America and Brazil. I mean the economic players as they change, how do they see their own opportunity?

MR. GEITHNER: You know it's a remarkable thing. You know we're just coming out of the worst recession that global economy's experienced in probably two generations. Every previous recession globally has either been precipitated by or has magnified or has produced really catastrophic financial crises across emerging markets including Latin America as a whole. This crisis is dramatically different.

You've had most of those economies saw less of a declining growth and are coming out of this quickly, look stronger now than they came in, much more resilient. And that's because they did a lot of things in the wake of the crisis of the 90s to build more stable financial systems to buildup a bunch of insurance against the risks of a bad recession like that, and to run their fiscal policy, monetary policy, much more prudently, and they've benefitted from that confidence. And it's a good thing.

MR. ROSE: Speaking of monetary policy, the last time you and I had a conversation, we talked of monetary policy in the role of the Federal Reserve. And the Wall Street Journal the next day editorialized about either respond to that or (b) tell me where you think monetary policy is?

MR. GEITHNER: Well, Charlie, we have a basic rule which is we don't comment on the judgments or independent Fed has to make. That's judgments they have to make and I'm pretty careful never to tread in that territory. I think the conversation you're referring to if I'm not mistaken was our conversation about what were the sources of the crisis, what caused it.

MR. ROSE: Exactly, they were.

MR. GEITHNER: And if I'm not mistaken what I said then, I think this is a fair judgment is that monetary policy around the world was too loose too long. And that helped contribute to this very sustained rise in house prices, asset prices, increase in leverage and borrowing, and did help sew the seeds of the crisis. Now it wasn't the only cause of crisis. You saw a bunch of regulatory failures, too. But it was a significant part of the crisis. And I think one of the things that governments--

MR. ROSE: [Interposing] Interest rates were too low for too long.

MR. GEITHNER: They were. Interest rates were too low too long, policy too loose too long. Now policy was tight here earlier than around the world, but because policy was loose elsewhere, you had a lot of money come from those companies into the United States pushing down interest rates, pushing up housing prices, asset prices, and I think one of the biggest challenges we face going forward is to try to get governments to do a better job earlier in containing those kinds of excesses.

And that excesses, that is very hard to do. And I think the dominate orthodoxy amongst central banks and supervisors in some ways is to say those are not things we can do, can't anticipate bubbles, don't know how large they are except in retrospect, can't really do much to take the air out of them preemptively, early, and that has been the dominate view of the conventional wisdom, and I think we're going to have to try to do a better job of catching these things earlier.

One of the things we try to set in place in the G20 process through this framework about growth was to try to force countries earlier to confront the potential implications having you know this basic pattern of merge where you have these big imbalances emerge, credit grow more rapidly, seeds of future crisis start to emerge. I think you'd like to find a way--we'd like to find a way to preempt those earlier.

MR. ROSE: I meant to talk about compensation and I forgot it for a moment, so I'm going to come back to it as we close this down. Mr. Feinberg [phonetic] works for you I think.

MR. GEITHNER: And he's doing an excellent job balancing impossible conflicting imperatives.

MR. ROSE: Which are?

MR. GEITHNER: Which are to and I'll say these starkly, which are to make sure that where institutions have had to take money from the government because they could not survive without it, that those resources are being used to get the company back on it's feet and repay the taxpayer.

We need to make sure the taxpayer gets their money back as quickly as possible. And we need to make sure that you know we're doing things that make it more likely credit gets flowing again to where it needs to in the economy. Those are difficult things to balance.

But as I said, I think he's doing an excellent job under remarkably difficult circumstances.

MR. ROSE: It only applies to certain companies. I mean do you worry that people who--is this partly because you want to thwart populous rage or because it's necessary, it's just a fair thing to do?

MR. GEITHNER: Charlie, what the President said in the joint session speech at the beginning of this year that you cannot govern in anger. The basic frustration Americans feel about the mess we're in and how basic unfair it is is completely understandable. They deserve to feel that way.

You know it's a stunning tragic failure of policy and judgment. But you know our job is to get this economy growing again and bring unemployment down to make sure there's credit flowing again, and to make sure we're creating a system less vulnerable to this in the future.

And so what drives our reform effort is to try to make sure we're changing how people are paid so you're not creating incentives for excess risk taking. And by shifting how people are paid, we think we can help reduce the odds of a future crisis. Now it's not the only thing.

It's maybe not the most important thing in terms of broad financial reform. But it's a necessary part of reform. It needs to be accompanied by these other things we talked about in terms of capital and disillusion, resolution authority. But it's the important thing to do.

MR. ROSE: The next big battle for you is regulation?

MR. GEITHNER: Regulation, we don't use these military terms, but since you used them, I'd say it's a war of necessity, not a

war of choice, and it's a just war. And we're going to achieve a strong package of reforms. For the reasons I said, it is the necessary fair thing to do.

How can you tell Americans, look them in the eye that after going through what they want through and still facing 10% of unemployment, and this enormous uncertainty about their future, that would leave in place, this is going to cause as much damage, it's like a completely untenable proposition.

And so I think we have a great responsibility to act now when people feel the searing memory of this crisis so strongly to put in place reforms that reduce risks this happens again, and I think we're going to get a good package of reforms. We've had a good, a very good couple weeks for reform. The House has already passed key components--

[Crosstalk]

MR. ROSE: Financial Services Committee.

MR. GEITHNER: I'm testifying on Thursday again. I think my 18<sup>th</sup> time since I've been in office.

MR. ROSE: That's a pleasant experience.

MR. GEITHNER: It is actually--it's actually, I'm not sure pleasant is the right word, but it's a necessary thing because we're doing you know these are difficult choices. You need to explain them, debate them. And it's the strength of our system that we force people to go through these things.

MR. ROSE: Thank you very much.

MR. GEITHNER: Nice to see you, Charlie.

MR. ROSE: Thank you.

MALE VOICE 1: Secretary Tim Geithner, thank you very much, especially coming down here, difficult day, taking the shuttle. We do appreciate it. We know it was hard. Charlie Rose, you did a wonderful job on two tremendous interviews we'll all remember. I want to thank all of you for being here.

[END TAPE ROSE GEITHNER]