Federal Financial Analytics, Inc.

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NEW PAPER SHOWS HOW FED POLICY INCREASES ECONOMIC INEQUALITY, CALLS FOR RAPID PORTFOLIO REDUCTION

New data and research show clearly that post-crisis Fed policy has played an important, if unintended, role widening the divide between the very rich and the rest of America. Many causes of economic inequality are deeply embedded in decades of change, but the Federal Reserve can and should reverse those due to its own actions with demonstrable inequality impact. Instead of the tentative path to portfolio reduction likely to be approved on Wednesday, the Fed should reduce its holdings in large, certain amounts on a predictable schedule at a far faster pace.

WASHINGTON, D.C., September 18, 2017 – On Wednesday, September 20, the Federal Reserve is likely to begin the portfolio reduction it announced in July. The Fed knows that reversing its unprecedented role as the largest U.S. investor will send ripples through global markets. What it has failed to recognize is what a new paper demonstrates: that this huge portfolio has also had dramatic impact widening the U.S. economic divide. As a result, the speed and pace of Fed portfolio reductions could be a force for equality if the Fed recognizes its role and finally acts on it. Just one week after U.S. income inequality hit another unprecedented high, the question is an urgent one addressed in a new paper released today by Washington consultancy Federal Financial Analytics, Inc. (FedFin).

The FedFin analysis mobilizes recent data and a raft of research – much of it buried within the

Federal Reserve itself – to show that the Fed's $4.5 trillion portfolio has unintended but still direct and devastating impact on the ever-wider divide between the very rich and the rest of America. The Fed's huge portfolio in concert with years of ultra-low interest rates is "unconventional" monetary policy. Unlike "conventional" policy that works through banks, this "quantitative easing" works through the markets to alter long-term asset prices in hopes of spurring employment. However, as this paper shows, employment is far from "full" even as the rich have grown far richer far faster than ever.

"The Fed's direct role in making the assets held by the richer more valuable might be acceptable if the Fed also achieved its goal of higher growth and employment. However, even Fed research shows that the cost of the Fed's portfolio to U.S. economic equality is far too high," said Federal Financial Analytics managing partner Karen Petrou. "Taking $4.5 trillion of low-risk assets out of the market hasn't spurred lending as the Fed hoped," she continued. "Instead, new data show clearly that investors are bidding up stock and bond prices. This will make wealthy investors a lot better off for a long time – assuming of course these price bubbles don't blow. But, low- and moderate-income Americans whose wealth, if any, comes from their homes, are falling farther and farther behind."

Charts in this paper show clearly how the Fed's policies in the wake of the crisis played a key role exacerbating wealth and income inequality in only the few short years since the 2008 debacle. The paper concludes that, "A certain, clear, and quick disposition plan with an out only for emergencies will in concert with higher rates reduce yield-chasing, normalize markets, and improve equality."

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