MEMORANDUM

TO: Federal Financial Analytics Clients

FROM: Karen Petrou

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On Wednesday, Rep. Ritchie Torres pressed Chairman Powell on several key points in my Monday *New York Times* opinion piece on the Fed's unintended, but important, economic-inequality impact. The chairman stoutly defended the Fed, at one point complaining that it could not be true that low rates increase wealth inequality because no low-income people have said so to the Fed. This is new – the Fed has never before announced a crowd-sourced policy construct. But, be that as it may, Mr. Powell's other points deserve a serious, substantive reply. In very short, it might be true that ultra-low rates enhance economic equality if they demonstrably improved income equality via gainful-employment increases large enough to offset growing wealth inequality resulting from the impact of negative real rates on small-dollar savings and broader financial dislocations. Problem is, this didn't happen from 2008 through 2021, long enough to tell.

Rep. Torres first quotes my article, correctly saying it asserts that ultra-low rates benefit investors, not savers. Without addressing what I was talking about – wealth inequality – Mr. Powell emphatically disagrees, saying that low rates "support a strong labor market." He then went on to take credit for "record" employment at the end of the last decade. But, even the Fed has since acknowledged that "employment" may well have been anything but record-breaking when employment is properly measured – see Mr. Powell's own *mea culpa* on that earlier this year.

And, of course, income equality isn't just about having jobs however the Fed chooses to count them. It also matters what one gets paid for working after taking inflation into account to determine real – not just nominal – income. Here, the Fed again falls flat: in 2001, inflation-adjusted households earned a median $57,930 that inched up only to $59,050 by 2019. This is of course infinitesimal and, while it's inflation-adjusted the way the Fed thinks about inflation, this paltry increase ignores huge spikes in housing, education, health-care, and many other costs that squeezed these families dry.

But, let's generously give Mr. Powell one for the moment on "record employment" because things were indeed picking up at the end of the last decade. Was this due to the decade of ultra-low rates that went before? No – plotting employment against rates shows that employment as the Fed judges it continued to rise even after the Fed started raising rates at the end of 2015. Thus, it's not at all clear that raising rates to enhance wealth equality would damage income equality.

Asked also by Mr. Torres about capital formation's crash through the last decade, Mr. Powell responds that:

> "I think businesses make rational decisions generally about what they should invest in and when they should give back to their shareholders. What that has to do with monetary policy is not clear to me."

Isn't it the prime directive of accommodative policy to spur lending that then leads to capital formation and lasting, high-wage jobs? If not for that, why are rates set ultra-low? Mr. Powell may be puzzled because ultra-low rates led to a corporate-borrowing binge without meaningful impact on productivity. Well he should be. If low rates are for capital formation, not capital distribution, then Mr. Powell needs to explain why we had so little of the first and so much of the second.

And finally, Mr. Powell says:

> "If you don't have a chance to take part in contributing to and then benefiting from the economy, then the economy is not all that it can be. Now, what can the Fed do? We can support maximum employment, that's what we can do."

Even if "maximum employment" is all by which one is to judge the Fed, then the Fed failed. As noted, "record employment" was anything but even if one charitably ignores real wage stagnation. And, if Mr. Powell reads his charter, he'll see that Congress also demands "full" employment so that anyone who wants a job gets one. This is an ambitious goal the Fed skirts with its "maximum" mantra, but Congress wants more, much more than the Fed delivered from 2010 onward. If one judges employment as Mr. Powell now espouses – by labor participation – then employment over the last decade was neither maximum nor full.

And, as my op-ed noted, the Fed's statutory mandate is a triple-header: full employment, price stability measured by the cost of consumption, and "moderate" interest rates. The Fed's got a long way to go.