

## A Nobel winner explains the big reason why the Fed should keep rates low

By [Jim Tankersley](#) August 26

Over the past year, Joseph Stiglitz has ramped up what is a rare campaign for an economist, particularly a Nobel laureate. He is pressuring policymakers, on the campaign trail and inside the Federal Reserve, to combat America's widening income inequality, which he has long called a massive economic concern.

Stiglitz and his team of researchers at the Roosevelt Institute (where he is the chief economist) produced a report earlier this year that Democratic candidates for president, including party frontrunner Hillary Rodham Clinton, have borrowed liberally from in their own policy plans. Today, he's releasing a [new paper](#) aimed at monetary policy makers, arguing that "the Fed has played a central role in the creation of inequality" and laying out several proposals to fix that — including delaying the interest-rate increase that most analysts had expected to come next month (at least before the recent global market turmoil broke out).

On Thursday, Stiglitz will take his message to a conference in Jackson Hole, Wyo, held by a group called the "Fed Up" campaign, in the shadow of an annual monetary policy conference that draws top monetary thinkers from around the world. He previewed that message in a phone interview with Wonkblog, which has been edited for length.

**Tankersley: The push to delay a rate increase, for inequality and other reasons, has been going on for a while. But we're at a particularly interesting moment in the global economy right now. How do recent events in markets change or amplify what you've been calling for?**

*Stiglitz:* It certainly amplifies it. One way of connecting the two things that have gone on is that, part of the hope for the robust recovery of the United States, in spite of the growing inequality and the fact that the middle is not doing very well, was that even if demand in the United States was going to remain weaker than it would have been because of the weak middle class, demand in emerging markets, including China, would fill the gap. What has been going on is a reminder that that may not work out in the way people had hoped. In fact, China may be contracting.

So it is both a commentary on the importance of this inequality and, in terms of the overall macro situation, a reminder that we live in a very precarious global situation where confidence that we're about to face inflationary pressures is very premature.

## **What can you say this week to get the attention of the Fed, in terms of timing of a rate increase?**

Before this week's turmoil, the big point we were trying to make is that – well there are two points. One is a broader theoretical issue about the Fed's impact on inequality, and my belief, and I think a widely shared one, that inequality is one of our country's major problems, and so the Fed ought to be sensitive to the impact its policies have on inequality.

One of the main ways, and even (Fed Chair) Janet Yellen has talked about this, is if that we have higher unemployment than we need, that not only causes more inequality among people who are unemployed, it also exerts downward pressure on wages for everybody, and the lower GDP that results means that states and localities have less revenues, so they have to cut back on public services, which are obviously more important to the people in the middle and on the bottom.

The second one is a more focused attention on precisely where we were in the business cycle and the asymmetric risk that we face. I don't think anybody sees significant inflationary pressures. So the standard argument for raising interest rates simply isn't there. There's been some discussion that, well, the labor market is tight, and well, eventually inflation will increase. (But) if you look at broader measures of the labor market, it isn't very tight, it isn't in a good situation, reflected in how wages are not keeping up with inflation, the low labor-force participation rate, the high long-term unemployment rate.

The key question is, what is the so-called natural unemployment rate – the rate at which unemployment starts? Back in the '60s, the United States had unemployment as low as 2, 3 percent without any inflationary pressures. We're nowhere near that. The question is, what is the natural rate? I think there is no compelling argument that it's 4.5, 5 percent. It could be three percent. Since we don't know, there's no reason to believe that pushing the unemployment rate lower than it is today will necessarily set off inflation.

## **Are Fed policy makers receptive to those arguments?**

As we know, the committee is divided. There are people who are inflation hawks and there are people who are concerned with unemployment, wages and the macro economy. That's why we're hoping to have some influence. As I said, the events of the last couple of days could have had more influence than anything I could say.

## **How much would a small initial rate increase, a quarter of a percentage point, actually affect the economy?**

That's a subject of a lot of discussion, in the following sense: The actual increase of the interest rate itself probably doesn't affect behavior that hugely (with a quarter-point rate increase). The issue is really what it does to the provision of credit, and to market expectations, and how those expectations get translated.

It is quite conceivable that given the short-sighted nature of markets, that when they actually raise interest rates, markets will come to believe that there's been somewhat of a bubble. If that were the only thing going on, the market might handle it reasonably well. But in the context of the world we live in, with China slowing down, the euro crisis continuing, the turmoil in commodity prices, all of which interact with each other, it could have significant effects on the stock market, as we've seen. Certainly it could have effects on stock-market volatility. All of which could lead firms to become a lot more cautious in their investment, and consumers in their consumption decisions, which could have the short-term effect of weakening the economy.

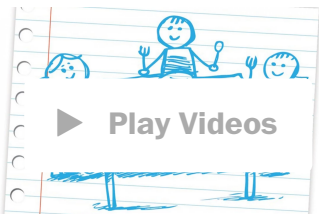
When our growth has been as volatile as it has been, when the stock market has been as volatile as it has been, when growth rate has been expected to be as weak as it is, and with all the weak signs, it would be undertaking undue risk.

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Jim Tankersley covers economic policy for The Post. He's from Oregon, and he misses it.

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