Bernanke Sees Need for Higher Household Spending to Fuel Growth

By Joshua Zumbrun - Mar 23, 2012

Federal Reserve Chairman Ben S. Bernanke said the U.S. economy is operating below its level prior to the financial crisis, and that increased household spending is needed to sustain the expansion.

“Consumer spending is not recovered, it’s still quite weak relative to where it was before the crisis,” Bernanke said yesterday in the second of four lectures on the history of the Fed that he plans to deliver at George Washington University. “In terms of debt and consumption and so on we’re still way low relative to the patterns before.”

The Federal Open Market Committee said in a statement after a March 13 meeting that subdued inflation and high unemployment still warrant holding the benchmark interest rate near zero at least through late 2014. Signs the economy is improving don’t dispel risks to growth that include rising gasoline prices, fiscal cutbacks and a weak housing market, New York Fed President William C. Dudley said on March 19.

Bernanke today plans to open a Fed conference in Washington involving policy makers from the U.K. and Japan that will focus on topics including new policy tools for fueling economic growth and challenges for central bankers.

The Fed chairman plans at 1:45 p.m. to give the opening speech at a two-day conference entitled “Central Banking: Before, During and After the Crisis.” Fed Vice Chairman Janet Yellen, Bank of England Governor Mervyn King, Bank of Japan Governor Masaaki Shirakawa and former European Central Bank President Jean-Claude Trichet are scheduled to speak.

Spur Growth

The conference will first consider a research paper by New York University Professor Mark Gertler saying the Fed’s asset purchase programs will help spur growth by reducing interest rates rather than by increasing the amount of reserves in the banking system.

Gertler, an adviser to the Federal Reserve Bank of New York who has co-written research with Bernanke, said in an interview yesterday that the economy may not need such a stimulus program at all.

“Inflation still appears to be contained so that’s good,” Gertler said in a phone interview. “Employment growth is picking up, so that’s good. It seems like the controls are at the right setting now.”

The unemployment rate was 8.3 percent in February, down from 9.1 percent as recently as August. The personal consumption expenditures index rose 2.4 percent in the 12 months through January, above the Fed’s 2 percent goal.

The Fed’s policy is “always subject to change as the news changes,” Gertler said. “But the economy is definitely picking up and inflation is contained and it seems like stimulus, at least from the Fed, is not appropriate now.”
Turning Point

Some policy makers say the Fed should hold off from more accommodation as the economy rebounds.

With policy currently “on pause, it may be a good time to take stock of whether we may be at a turning point,” Federal Reserve Bank of St. Louis President James Bullard said in a speech in Hong Kong. “As the U.S. economy continues to rebound and repair,” further action “may create an overcommitment to ultra-easy monetary policy.”

Economic reports yesterday added to evidence the world’s largest economy is gaining strength.

The number of Americans saying the economy is getting better rose in March to the highest level since 2004. Thirty- four percent of respondents to Bloomberg’s monthly consumer expectations survey said the economy was improving, the largest share since January 2004.

Leading Index

The index of U.S. leading indicators rose in February by the most in 11 months, the Conference Board said. Applications for unemployment benefits dropped last week to the lowest level in four years, a Labor Department report showed.

U.S. stocks retreated, trimming the longest monthly rally since September 2009 for the Standard & Poor's 500 Index, as manufacturing contracted in China and Europe and FedEx Corp. tumbled amid a disappointing forecast.

The S&P 500 declined 0.7 percent to 1,392.78 at 4 p.m. New York time, slumping 1.2 percent in three days. The gauge has risen 2 percent in March, on pace for a fourth monthly rally.

Bernanke said yesterday the central bank's interest-rate policies last decade weren’t responsible for the housing price bubble that led to the recession.

“Some have argued that the Fed’s low interest-rate monetary policy in the early 2000s contributed to the housing bubble, which in turn was a trigger of the crisis,” he said.

Overseas Booms

“Most evidence suggests otherwise,” Bernanke said, focusing on history and not on current monetary policy or the economic outlook. In defense of the Fed, Bernanke cited house price booms in foreign countries and said the size of the asset bubble was too large to be explained by changes in mortgage rates. Also, home prices began to rise in the late 1990s, before the Fed lowered rates, he said.

Bernanke, a former economics professor at Princeton University, is returning to the classroom this week and next to explain the central bank’s actions during the financial crisis and the longest recession since the Great Depression. His lesson yesterday is titled “The Federal Reserve after World War II.”

Following a recession in 2001, the central bank lowered interest rates to 1 percent in 2003 and 2004 even as home price gains accelerated. Bernanke’s defense of the Fed actions drew on a January 2010 speech he gave in Atlanta, he said.

Though its interest-rate policies were appropriate, Bernanke said, the Fed “made mistakes in supervision and regulation.”
Bank Supervision

“In our supervision of bank and bank-holding companies we didn’t push hard enough on this issue of measuring your risks,” Bernanke said. “Another area where the Fed performed poorly was I think in consumer protection.”

Bernanke, 58, also said government policies to increase homeownership were not principally to blame for the housing bubble.

“I think to put it all on the government is probably wrong,” Bernanke said in response to student questions. “Most of the worst loans were made by private sector lenders and then sold through private-sector securitizations. They didn’t touch Fannie or Freddie,” he said, referring to government-sponsored entities Fannie Mae and Freddie Mac.

While his lecture focused on historical topics, Bernanke noted that today’s policy benefits from the low inflation brought about as the result of former Fed Chairman Paul Volcker’s battle against price increases.

“After a long period of low inflation most people are pretty comfortable that inflation will stay reasonably low,” Bernanke said. “And that helps a lot” since “with inflation staying low the Fed has more leeway.”

In response to a question about Fed transparency, Bernanke said “most of the time transparency can make monetary policy work better” and promote accountability of the central bank.

Bernanke plans to speak on March 27 and March 29 about the Fed’s response to the financial crisis and the ensuing recession. The lecture series will be streamed live on the Fed’s website and on ustream.tv.

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