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SHUT UP, SAVERS!

by James Surowiecki APRIL 8, 2013

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Ben Bernanke may look like a mild-mannered academic, but, according to a chorus of critics, the chairman of the Federal Reserve is one of history's great thieves. Over the past four years, the Fed has kept interest rates near zero and has pumped money into the economy by buying trillions of dollars in mortgage-backed securities and government debt. The idea is that a so-called "loose" monetary policy can help galvanize a weak economy—for instance, by encouraging businesses to invest and hire and by making it easier for people to buy homes. But, to his detractors, Bernanke is guilty of waging a "war on savers"—fleecing people, especially retirees, of hundreds of billions of dollars that they could have earned in interest. Among many conservatives, this notion has become mainstream. Last year, both Mitt Romney and Paul Ryan regularly attacked the Fed for keeping interest rates too low, and, when Bernanke testified before Congress in

February, Senator Bob Corker, of Tennessee, upbraided him for "throwing seniors under the bus."

Certainly, it's not the easiest time to live off interest income. The average rate on a savings account is less than 0.25 per cent. Long-term certificates of deposit offer rates well below inflation, and even a ten-year government bond yields less than two per cent. No wonder people with lots of savings want the Fed to start tightening—to stop buying bonds, and to raise interest rates. But most Americans depend on wages and salaries for their livelihood, not on interest income, and higher interest rates would hurt the job market, which is still weak, with unemployment near eight per cent and wages barely rising. Also, most Americans have more debt than savings, which means that they benefit directly from lower interest rates. Only an estimated seven per cent of all financial assets nationally are directly held in interest-bearing assets (like CDs or savings bonds). Even seniors, one of the groups most obviously hurt by low interest rates, get only ten per cent of their income from interest payments. Bernanke has been accused of waging class warfare and forcing senior citizens to eat cat food, but the simple fact is that people who are net savers are, on average, wealthier than those who aren't.

And what if the Fed did raise interest rates? It's unlikely that savers would be better off in the long run, since the move would slow down the economy as a whole and perhaps even tip us back into recession. Most savers aren't just savers, after all: they are also workers or homeowners or stock-market investors—groups that need a growing economy to prosper. Even people who live entirely off interest rely on economic growth. "There's this myth that monetary policy is a zero-sum game," Scott Sumner, an economist at Bentley University who has become an influential advocate for a more expansionary Fed policy, says. "But it's perfectly possible that looser monetary policy could make both savers and borrowers better off. When the economy is weak, tight money makes the whole pie smaller. When the economy is robust, we get more output, which means more real income, and that usually means higher rates of return for investors." Indeed, the biggest culprit when it comes to low interest rates isn't the Fed: it's the weak economy, which has held down the demand for credit and made us all risk-averse. That's why interest rates are low across most of the developed world—even in countries where central bankers haven't been buying up assets the way the Fed has.

The war-on-savers crowd makes Bernanke out to be a wild-eyed ideologue, willfully risking hyperinflation and sacrificing the well-being of retirees to his reckless schemes. But, if you look at the U.S. economy, you don't see any of the signs you'd expect if the

Fed were acting recklessly: the money supply is not growing rapidly, and inflation is trivially low. If anything, Fed policy has been too cautious; it could have done more to rev up the economy. Sumner has argued that the Fed could have set a public target for nominal G.D.P. and committed itself to printing as much money as needed to get there. And a new research paper from the New York Fed suggests that we should have aimed at a higher rate of inflation, which would have stimulated spending and investment by making it less attractive to just park money in the bank. Bernanke's critics like to point to the still weak job market as evidence that the Fed's policy hasn't worked. It's far more likely evidence that the Fed hasn't gone far enough.

It's easy to understand why savers feel like collateral damage in the Fed's fight against recession, but too much sympathy for their plight is dangerous. Sumner points out that, in the past century, there have been only five occasions when a central bank tried to end a zero-bound-interest-rate policy. On four of those occasions, the central bank acted too soon, the economy slipped back into recession, and rates had to be cut all over again. "Raise rates now," Sumner says, "and you can quickly turn what looks like a recovery into a double-dip recession." Currently, the big risk isn't that the Fed will wait too long to raise interest rates; it's that pressure from savers will cause it to raise them prematurely. The economy may be looking a bit perkier, but it's still growing slowly, and it has an enormous amount of ground to make up; median household income, for instance, is still seven per cent lower than it was before the recession. It may be hard for people to live off their savings these days, but the far more urgent problem is that it's even harder for people who don't have jobs, or whose wages are stagnant, to save anything at all. ♦

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