

POLITICS & ECONOMICS

Fed Chief Warns of Widening Inequality

Bernanke Cautions That Some Fixes Could Hurt Market
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 By DAVID WESSEL 2/1/07

WASHINGTON—Federal Reserve Chairman Ben Bernanke cautioned that widening economic inequality may make Americans “less willing to accept the dynamism ... so essential to economic progress.” But he warned politicians to avoid responses that would make labor markets less flexible or create barriers to international trade and investment.

In an unusual speech for a central banker, Mr. Bernanke said a wiser approach to the problem would be to improve education and training and to cushion dislocations caused by technology and globalization. He cited such steps as making health and pension benefits more portable and offering retraining and job-search assistance to displaced workers.

Mr. Bernanke's comments at the Greater Omaha Chamber of Commerce add to a chorus of concern about widening economic inequality from top government officials, including President Bush, Treasury Secre-

tary Henry Paulson and Mr. Bernanke's predecessor, Alan Greenspan, as well as prominent Democrats.

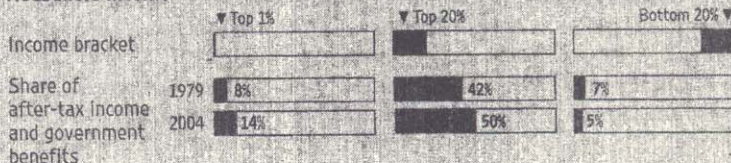
Wandering beyond the boundaries of monetary policy, his area of responsibility, Mr. Bernanke said: “Although average economic well-being has increased considerably over time, the degree of inequality in economic outcomes has increased as well ... for at least three decades.” A text of his speech was released by the Fed in Washington.

In his 15-page lecture, complete with 48 academic references, Mr. Bernanke documented the inequality evident in data on wages, household incomes and even baseball players' contracts. He also examined economic forces behind the trend, from changes in technology that have increased employers' appetite for more-educated workers, to the decline of unions, to the surge in chief executives' salaries, to the impact of globalization. He said the effect of the latter has been “moderate and almost surely less important than the effects of ... technological change.”

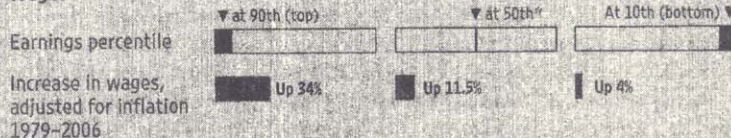
The Inequality Facts

Evidence of inequality cited by Fed Chairman Bernanke

Household Income



Wages



*Statistical middle

Source: Federal Reserve

◆ **The News:** The Fed's chief warns widening economic inequality may sour Americans on the dynamism “so essential to economic progress.”

◆ **The Background:** Growing evidence of widening gap between economy's winners and losers.

◆ **The Prescription:** Mr. Bernanke cites education, aid to displaced workers.

The Fed chairman noted that in professions ranging from entertainment to investment banking, the forces of globalization and technological innovation have increased the value of the most-talented individuals—the “superstars”—over the merely good. “Two decades ago, the highest-paid player for the Boston Red Sox (and in the Ameri-

can League), Jim Rice, earned (in inflation-adjusted terms) just over \$3 million. In 2004, the highest-paid player on the Red Sox (and in all of major-league baseball) was Manny Ramirez, who received \$22.5 million for the season.”

“The number of fans who can fit into Fenway Park has not increased much ... presumably the Red Sox owners believed that Ramirez's highest salary was justified by the increases in broadcast and merchandising revenues he might generate as a result of the confluence of new distribution channels (such as Internet-based broadcasts of games) and a larger and wealthier potential global audience,” he added.

Mr. Bernanke spoke explicitly about the degree and causes of inequality, and more carefully about the increasingly loud political debate over what, if anything, to do about it. “Firm conclusions about the extent to which policy should attempt to offset inequality ... are properly left to the political process,” he said.

But he offered three principles that he said are “broadly accepted in our society”—economic opportunity should be as widely distributed and equal as

possible, economic outcomes needn't be equal but should be linked to a person's contributions, and people should get some insurance against very painful outcomes.

“We ... believe,” he said, referring to Americans generally, “that no one should be allowed to slip too far down the economic ladder, especially for reasons beyond his or her control.”

Mr. Bernanke, who served briefly as an economic adviser to Mr. Bush before becoming Fed chief a year ago, avoided any mention of tax policy, a favorite tool of Democrats interested in reducing the inequality produced by market forces. He noted that eliminating inequality altogether would be unwise.

“Our market-based economy, which encourages productive activity primarily through the promise of financial reward, would function less effectively,” he argued. The dynamism that has propelled the U.S. economy for decades brings with it “painful dislocations” for some workers, he added. But he said, “If we do not place some limits on the downside risks to individuals ... the public at large might become less willing to accept the dynamism that is so essential to economic progress.”

When Mr. Greenspan was Fed chairman, he occasionally expressed concern about the widening gap between winners and losers in the American economy, though usually in response to questions from members of Congress, rather than in public speeches. At the Joint Economic Committee in June 2005, for instance, Mr. Greenspan observed “As I've often said, this is not the type of thing which a democratic society—a capitalist democratic society—can really accept without addressing.”

Mr. Greenspan generally attributed the disparities to the extra wages that employers pay more-educated workers. Mr. Bernanke acknowledged that is a major factor, but not the only one.