THE DAILY CALLER

Banking committee clears the way for continuing flawed Fed policies

By: Mark Calabria - November 22, 2013

Lost in Thursday's "nuclear" attack on the Senate, the Banking Committee approved the nomination of Janet Yellen to succeed Ben Bernanke as chair of the Federal Reserve. Even without the filibuster changes, her nomination was all but guaranteed. Once confirmed she will almost surely continue the Fed's current reckless policies.

The Banking Committee approved Yellen 14 to 8, with only one Democrat, Sen. Joe Manchin (D-W.Va.), voting against her and she is likely to be voted on by the full Senate by the middle of December.

Unlike Supreme Court nominees, who generally receive days of questioning by the Senate, the Banking Committee checked its box on "advise and consent" in just over two hours. Despite that low bar, the full floor debate is likely to be even more devoid of substance.

Yet the risks to our economy demand such a debate. Prior to her service as the Fed's Vice Chair, Janet Yellen led the San Francisco Fed from 2005 to 2010. The San Francisco district includes, in addition to California, both Nevada and Arizona. Its fair to say Yellen's backyard was ground zero for the housing bubble, and it appears she was completely blind to it.

Looking at Yellen's statements, and the San Francisco Beige Book reports, one is hard pressed to see any concern coming from Yellen. In fact we repeatedly see mortgage credit being described as "good" in the San Francisco reports.

At worst, she shared the widely held view that the bubble was actually a positive, because it had the appearance of creating wealth (like today's stock market), while also appearing to do something about the labor market. This is the real danger: That rather than see the housing bubble as a "bug" to be fixed, she viewed it as a positive feature of the Fed's monetary efforts.

Discussions about monetary policy often focus on whether current Fed policy is expansionary or contractionary. Lost in this debate is that it can be both. While the Fed has injected considerable liquidity into the banking system, it has also paid banks, via interest on reserves, not to lend. It would be nice if the Fed could at least decide upon what exactly it is trying to achieve. Unfortunately, such confusion is likely to continue under Yellen.

With the bank rescues of 2008 and the Dodd-Frank Act expansion of Fed powers, the Fed continues to be the most important U.S. bank regulator. While it was encouraging to hear Yellen recognize the importance of dealing with too-big-to-fail, it was discouraging for her to omit the Fed's role in having created it.

As long as we continue to have a bank regulatory regime of unfettered discretion, who occupies the regulatory chairs matters. Unfortunately, Yellen appears wed to former Treasury Secretary Timothy Geithner's approach to bank regulation: rescue first and ask questions later. Congress and the public will have to keep her feet to fire to avoid future bank rescues.

No one denies Yellen's academic qualifications, but those are ultimately irrelevant. Arthur Burns was widely recognized as the Ben Bernanke of his day, and his tenure as Fed Chair was a disaster because, as admitted by Burns himself, the Fed lacked the will to make hard choices. It took Paul Volcker to make those hard choices, but it is important to remember that those choices were not popular ones. Ultimately Janet Yellen will have to decide whether she's going to be Arthur Burns or Paul Volcker.