

Title: "Greenspan's Bubbles: The Age of Ignorance at the Federal Reserve"  
Author: William A. Fleckenstein (with Frederick Sheehan)  
Publisher: McGraw Hill  
Length: 194 pages  
Price: \$21.95 (hardcover)  
Reading time: 3 hours  
Reading rating: 3 (1 = very difficult; 10 = very easy)  
Overall rating: 1 (1 = average; 4 = outstanding)

### The Symptomatic Greenspan

One gets the impression from reading "Greenspan's Bubbles: The Age of Ignorance at the Federal Reserve" that the last 19 years have been an unmitigated economic disaster. I profoundly disagree, to the point of wondering how anyone with any knowledge of U.S. economic history could hold such a view.

Don't get me wrong – I share most of Fleckenstein's criticisms of the Federal Reserve system. He has a number of good, accurate lines about the problems with central banking itself. For instance, he notes that the Federal Open Market Committee (FOMC) is essentially a Soviet-style central planning board, and such committees are historically notorious in their failures. Further, Fleckenstein argues, when the Fed makes mistakes its only recourse is to use the same flawed process to fix its mistakes. Yet, as he says, "they seem happy to do it." (p. 4)

Fleckenstein also recognizes that for any modern central bank, inflation is the norm: "[I]t is not deflation that presents a problem. The reality is that governments will cheat their citizens over time with inflation." (p. 142) This is true and under-appreciated.

Unfortunately, aside from a handful of those lines, "Greenspan's Bubbles" directs the vast bulk of its criticism at one man (thus, the title). More unfortunately, for all the talk about Greenspan making bad decisions, far less is said about actual changes in rate targets than is said in complaint about Greenspan's rhetoric. I am surprised that someone could read the many quoted passages from Greenspan's congressional testimony and FOMC meetings and come away with a clear enough idea of what was said to actually be upset by it.

In terms of Fed policy under Greenspan, the book makes two key claims: lowered target rates in the mid 1990s caused a stock bubble and lowered target rates starting in 2001 caused the housing bubble. The bulk of the book is a ranting, but unconvincing explanation of the first bubble, with a shorter, but more persuasive explanation of the second. For the stock bubble, the only clear pattern is that the Fed targeted lower rates during recessions and raised them again afterward. The book fails to give a detailed timeline of Fed policy, but the move was toward lower rates in 1991 and 1992 and increased rates in a slow, steady fashion in 1994. The rest of the 1990s was a series of small changes back and forth around 5.25 percent.

The author insinuates that a rate-cutting frenzy occurred during the 1990s, but the actual changes back and forth during that decade do not make a strong case for the creation of a stock bubble. Yes, the Federal Funds Rate fell almost four percentage points during 1991 and 1992; but the target was raised another 3 percent in 1993.

The housing bubble is a different story. Starting in January 2001, the Federal Funds Rate target of 6 percent was slashed to just 1 percent over a relatively short period of less than three years. Fleckenstein gets this one right: extremely aggressive monetary policy comes at a cost, and one of those costs is more high-risk loans.

In essence the author criticizes the Fed, and Greenspan in particular, for doing what most economists expect the Fed to do – provide a "soft landing." But if attempts to smooth out the process of creative destruction cause so many problems, then it seems to me that Greenspan is a symptom, not the source of the flaws in the Federal Reserve system. Fleckenstein's real target should be the institution of central banking itself, rather than one central banker.

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