Fed Chairman Pops The Big Question: Is Market Too High?: But ...
DAVID WESSEL Staff Reporter of THE WALL STREET JOURNAL
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But Greenspan Waffles When It Comes to an Answer, Despite Concern Over Rise

By DAVID WESSEL
Staff Reporter of THE WALL STREET JOURNAL

WASHINGTON — Federal Reserve Chairman Alan Greenspan tiptoed up to a big question last night: Is the stock market overvalued? But he didn't answer it.

"How do we know when irrational exuberance has unduly escalated asset values, which then become subject to unexpected and prolonged contractions as they have in Japan over the past decades?" Mr. Greenspan asked in a speech at the American Enterprise Institute. "And how do we factor that assessment into monetary policy?"

The answer, however, was characteristic Greenspan. He noted that sustained low inflation tends to be good for stock prices. He pointed out that the Fed wouldn't worry about "a collapsing financial asset bubble" if it didn't hurt the economy. He recalled that the 1987 stock market crash had "few negative consequences for the economy."

But then, as he came closer to giving his views on the rhetorical question he posed, the language got murkier. The Fed "should not underestimate or become complacent about the complexity of the interactions of asset markets and the economy," he said. He added that "evaluating shifts" in prices of stocks and other assets "must be an integral part of the development of monetary policy." And then he changed the subject.

Inside the Fed, Mr. Greenspan is known to have concerns about the stock market's surprisingly rapid rise. But given the current state of the economy, the Fed isn't likely to raise interest rates in order to dampen the exuberance on Wall Street.

Delivering a detailed description of the central bank's role in a democratic society, Mr. Greenspan defended his eclectic approach to making monetary policy. "We are led, of necessity, to employ ad hoc partial models and intensive information analysis," he said. "There is no alternative to this."

For a time in the early 1980s, the Fed used the money supply as a major gauge. But the relationship between the money supply and the economy broke down in the 1990s, Mr. Greenspan has said. He said last night that there are "some indications" that the link between the money supply and the economy "may be coming back on track," but he said flatly that the Fed cannot "in the future expect to rely a great deal on money supply in making monetary policy."