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The following *New York Times* article, published on August 28, 2011, presents commentary on the Federal Reserve's actions during the past few years, including the lack of any statement last week at the Jackson Hole, Wyoming, annual conference. There are many pros and cons of any further action by the Federal Reserve, some of which we will study later in the course.

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Dissecting the Mind of the Fed

By **DAVID LEONHARDT**

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Washington

IF you were to conduct a survey of the country's top economists, you would find a fair number who did not believe that the Federal Reserve should be taking more aggressive steps to help the economy. Some would worry that injecting more money into the economy might unnerve global investors or set off uncontrollable inflation. Others would wonder whether, with interest rates already so low, the Fed even had much power to lift economic growth.

But you would also find a sizable group of economists who thought the Fed could and should do far more than it was doing. This group, known as doves, tilts liberal, though it includes conservatives as well. If anything, it can probably claim a larger number of big-name economists — J. Bradford DeLong, Paul Krugman (an Op-Ed columnist for The New York Times), Christina D. Romer, Scott Sumner and Mark Thoma, among others — than the camp that believes the Fed has done too much.

You would never know this, however, from listening to the public debate among Federal Reserve officials. That debate is much narrower.

On one side are people like Ben S. Bernanke, the Fed chairman, who defend both what the Fed has done and what it hasn't done. On the other side are the so-called inflation hawks, who say the Fed has been far too aggressive. Rick Perry, the Texas governor and arguably the Republican presidential front-runner, offered a particularly blunt version of this criticism when he recently accused Mr. Bernanke of flirting with treason.

Last week's annual Fed retreat in Jackson Hole, Wyo. offered the latest illustration of the debate's contours. After months of disappointing recent economic data, the Fed chose not to take major action. Instead, Mr. Bernanke defended the Fed's modest Aug. 9 announcement that it planned to hold down short-term interest rates until mid-2013.

The only public criticism of that move from within the Fed came from three hawks who voted against it, which made for the most dissents on its policy-setting committee in almost 20 years. No Fed official, by contrast, has recently dissented out of the belief that the Fed has been too timid, and no one presented a paper in Jackson Hole making that case either. For now, the Fed debate — at least the open debate — is one between inflation hawks and moderates, with nary a true dove in sight.

It is obviously impossible to know precisely which policy would be the best one for the struggling American economy. A dovelike injection of money into the economy would have the potential to increase incomes and inflation in a benign way, effectively reducing household debt burdens, giving people more confidence to spend money and eventually spurring hiring. But further action also brings some risk of setting off uncontrollable inflation, which, while very low historically, has been rising lately.

No doubt, some of this richer hawk-dove debate is occurring behind closed doors at the Fed and in Jackson Hole. But the public conversation still matters. It affects nothing less than the Fed's credibility. Mr. Bernanke knows that if he errs on the side of passivity — worrying more about inflation risks than unemployment — he risks only a modest flogging from colleagues and politicians. If he leans the other way, he risks being accused of, well, treason.

That difference has almost certainly affected Fed policy, causing it to be less aggressive on policy and more optimistic about economic growth than it otherwise would be. As Mr. Thoma, an economics professor at the University of Oregon, recently wrote, Fed officials are "in a more precarious political position than they ever expected to be in." With the benefit of hindsight, we also know that the Fed has been too optimistic during the past two years, forecasting stronger growth than ultimately occurred.

Why does the Fed skew more hawkish than the economics profession as a whole? Part of the answer lies in the way the 12 voting members of the policy-setting committee are chosen. They are a mix of presidential nominees subject to Senate approval, with 14-year terms, and regional Fed presidents, who are chosen by outside boards that are made up partly of private-sector finance executives.

David Levey, a former managing director at Moody's and another critic of Fed inaction, points out that banks often have more to lose from inflation than from unemployment. Inflation reduces the future value of the money that their debtors — homeowners, car buyers, small businesses and the like — will repay them.

"The Fed regional banks represent, in essence, the banking community, which tends to be very conservative and hawkish," Mr. Levey says. "Creditors don't like inflation — it's good for debtors." Indeed, the three recent dissents all came from regional bank presidents: Richard W. Fisher of Dallas, Narayana R. Kocherlakota of Minneapolis and Charles I. Plosser of Philadelphia.

Mr. Obama, for his part, has chosen to nominate mostly moderates, rather than strong inflation doves. Most significantly, he re-nominated Mr. Bernanke, originally a George W. Bush adviser and appointee, to a second four-year term as chairman, based largely on Mr. Bernanke's aggressive steps in 2008 and 2009 to prevent another depression. The Obama administration has also been slow to fill some Fed openings. At least one of the 12 seats has been vacant since Mr. Obama took office, and two are now.

The doves outside the Fed do not all favor the same steps — or even the label dove. Indeed, they have some significant disagreements.

Some want a more aggressive round of quantitative easing, a policy the Fed enacted in 2009 and 2010 to try to bring down long-term interest rates. Some want significantly faster near-term inflation, to make up for the low inflation of the past few years and give people an incentive to spend more money now. Some want the Fed to commit to buying up financial assets — the functional equivalent of printing money — until the nation's gross domestic product has recovered from the crisis. In Sweden, the central bank has engaged in more aggressive asset buying, which appears to be one reason the economy there has recovered from the crisis much better than in most other rich countries, notes Mr. Sumner, a conservative-leaning monetary-policy economist at Bentley University.

But the doves do want the Fed to move in the same direction: toward making a more energetic attack on unemployment. Mr. Sumner has become so dispirited by the Fed that, before leaving on a trip for Italy last week, he left a post on his well-read blog, The Money Illusion, under the headline, "Not enough." The headline, he wrote, "refers to my reaction if the Fed does something while I'm gone."

Whatever one thinks of his prescription, his prediction was spot on. Mr. Bernanke concluded his Jackson Hole speech by urging other branches of government to improve their economic policies. The one Fed change he announced was a lengthening of next month's monetary-policy meeting to two days, up from the usual one, "to allow a fuller discussion" of the issues.

Outside the Fed's walls, of course, that fuller discussion has already been under way for a long time.