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The Fed's Advice and Dissent
Professor Sanjay Chugh
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The "Finance and economics" article in the November 8, 2014 issue of *The Economist* documents that long-time "inflation hawks" Richard Fisher (the soon-retiring President of the Federal Reserve Bank of Dallas) and Charles Plosser (the soon-retiring President of the Federal Reserve Bank of Philadelphia) were glad to formally end "QE3" in the FOMC meeting in late October 2014. Perhaps more surprisingly, Narayana Kocherlakota (President of the Federal Reserve Bank of Minneapolis) was the lone dissenter, preferring to keep QE3 going. This was perhaps surprising because Kocherlakota has long been a leader of the "RBC-style" school of thought (as was, coincidentally, Plosser).

Kocherlakota has been typically more inclined towards the "Freshwater School" of economics, whose base is located around the (freshwater) Great Lakes (e.g., the University of Chicago and the University of Minnesota). In contrast, the base of the "Saltwater School" of economics is concentrated near the (saltwater) Atlantic Ocean (e.g., MIT, Harvard, and Princeton).

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The Federal Reserve

Advice and dissent

The Fed mollifies its hawks but now its doves are fretting

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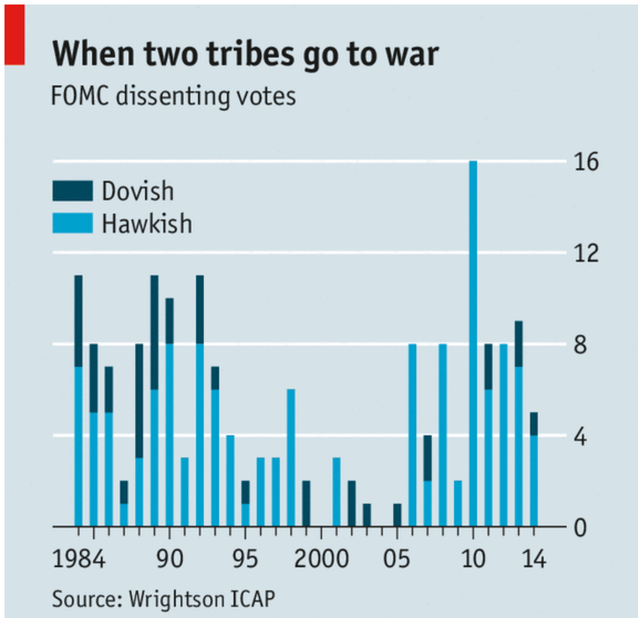

IN HIS nine years as president of one of the Federal Reserve's twelve regional branches, in Dallas, Richard Fisher has voted against the Fed's monetary policy eight times, always in favour of a tighter stance. Not one to let his vote speak for itself, Mr Fisher has compared the Fed's bond purchases to bourbon served to an alcoholic, "dry inflationary tinder" and water pouring over the "the gunwales of the ship of our economy."

So few were as happy as Mr Fisher when the Fed last month decided to bring its third round of bond buying (known as "quantitative easing") to a halt. He and his fellow hawk, Charles Plosser, president of the Philadelphia Fed, registered their approval by not dissenting. Rather, the locus of opposition shifted to the doves, in the form of Narayana Kocherlakota, the president of the Minneapolis Fed, who wanted more bond buying and a stronger commitment to getting inflation higher.

The Federal Open Market Committee (FOMC), which votes on monetary policy, is normally composed of the Fed's seven Washington-based governors plus the presidents of the regional banks, of whom five vote: New York's, and four others in rotation. Policy recommendations are formulated mainly by Janet Yellen, the chair, working closely with Stanley Fischer, the vice-chair, and Bill Dudley, the president of the New York Fed. Ms Yellen and Mr Dudley are dovish, Mr Fischer more of a centrist. In practice, though, Ms Yellen strives for consensus, which means sometimes shading her views of economic developments to accommodate her colleagues'.

That job has got harder in recent years as FOMC members have dissented with growing frequency (see chart) and verbosity. Mr Kocherlakota, for instance, has dissented twice this year and issued explanatory statements shortly thereafter. Dissenters seldom change the direction of policy; this is especially true of serial dissenters such as Messrs Fisher and Plosser, whose warnings of inflation have found little resonance with their colleagues or in the data. Yet their influence is still felt outside the Fed, thanks to changes in how the central bank conducts itself. Its use of forward guidance to steer bond yields empowers officials who talk more.

In 2013, the two officials other than the chairman who moved the market most were Mr Fisher and James Bullard, president of the St. Louis Fed, because they spoke so much, according to Macroeconomic Advisers, a forecasting outfit. Dissenters' impact has also been enhanced by the publication each quarter of officials' forecasts of interest rates over the next two to three years. Each forecast is represented by a dot on a chart. Because the dots are anonymous, a shift in the dots is taken as representing the entire Fed when it may in fact simply be the outliers. Such a shift jolted the market in September.

Given that, the fact that both Mr Plosser and Mr Fisher are retiring next year ought to make Ms Yellen's job easier. However, that will depend on who replaces them, a decision in the hands of their banks' boards, and more importantly, who will fill two vacant governors' seats. Barack Obama has yet to nominate anyone, but he has been pressed to nominate a community banker and someone with regulatory expertise.

The Republicans take control of the Senate in January; they will probably reject any nominee they consider too dovish. Also in January, Jeffrey Lacker, president of the Richmond Fed, will get a vote. Mr Lacker is even more hawkish than Mr Fisher, having dissented 13 times in his time on the FOMC. Ms Yellen will have her work cut out.

From the print edition: Finance and economics