Narayana Kocherlakota: Opening remarks

Speech by Mr Narayana Kocherlakota, President of the Federal Reserve Bank of Minneapolis, at Carroll College, Helena, Montana, 4 September 2014.

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Thanks for the introduction, Tom. It's a pleasure to be back in Helena – the site of the only branch office of the Federal Reserve Bank of Minneapolis.

I'll kick things off with some basics about the Federal Reserve System and some thoughts about Fed history. But the plan is for us to spend the bulk of our evening on your questions. One key point before I proceed: The views I express today are my own and are not necessarily those of others in the Federal Reserve System, including my colleagues on the FOMC.

In terms of basics about the Fed: I like to tell people that the Fed is a uniquely American institution. What do I mean by that? Well, relative to its counterparts around the world, the U.S. central bank is highly decentralized. The Federal Reserve Bank of Minneapolis is one of 12 regional Reserve Banks that, along with the Board of Governors in Washington, D.C., make up the Federal Reserve System. Our bank represents the ninth of the 12 Federal Reserve districts and includes Montana, the Dakotas, Minnesota, northwestern Wisconsin and the Upper Peninsula of Michigan.

Eight times per year, the Federal Open Market Committee – the FOMC – meets to set monetary policy over the next six to seven weeks. All 12 presidents of the various regional Federal Reserve banks – including me – and the governors of the Federal Reserve Board contribute to these deliberations. However, the Committee itself consists only of the governors, the president of the Federal Reserve Bank of New York and a rotating group of four other presidents. I'm one of those four presidents this year. In this way, the structure of the FOMC mirrors the federalist structure of our government, because representatives from different regions of the country – the various presidents – have input into FOMC deliberations.

This basic federalist structure has a long history. In fact, this year is the centennial of the opening of the 12 Reserve Banks and the start of the work undertaken by the Federal Reserve System. It's been a fascinating hundred years, with many twists and turns along the way. I'm sure that many of you have questions about that journey. The answers to all of your questions – and probably more – are on a website that the Fed has created at federalreservehistory.org. I encourage you to visit this site to learn more about the people, places and events that have shaped Federal Reserve history. I'd especially encourage you to look up Norman Holter. Mr. Holter was one of the original directors of the Minneapolis Reserve Bank, and he played the key role in a branch office being established here in Helena in 1921.

I've always enjoyed reading and studying history. And I strongly believe that history can help inform policymakers' decisions in the current day. But, at the same time, I do think that policymakers need to be careful in how they use history. The monetary history of the 1970s is a great example of this need for care. I'm sure that some of you in this room remember that inflation – the rate of growth of prices – rose to disturbingly high levels in the 1970s. Faced with this challenge, President Ford launched a national campaign to "Whip Inflation Now" – WIN for short. The famous Broadway composer Meredith Willson wrote a song for the WIN campaign in which he summarized the economic situation in these catchy lyrics: "Who needs inflation? Not this nation! Who's going to pass it by? You are and so am I!"

Mr. Willson's pithy characterization was spot on in 1974. But 40 years later, I would suggest that it's exactly backward. Right now, this nation *needs* more inflation. The Federal Reserve aims to keep the personal consumption expenditure (PCE) inflation rate at 2 percent. But since the start of the recession almost seven years ago, the PCE inflation rate has averaged 1.5 percent. Over the past year, it has averaged 1.6 percent. And I expect it to remain below 2 percent until 2018.

The persistently below-target inflation rate is a signal that the U.S. economy is not taking advantage of all of its available resources. If demand were sufficiently high to generate 2 percent, then demand would be sufficiently high to allow the economy to make use of the underutilized resources. And the most important of those resources is the American people. There are many people in this country who want to work more hours, and our society is deprived of their production.

So, it's fun and educational to read about the 1970s on the Fed history gateway. I encourage you to do so. But it's critical for monetary policymakers like myself to realize that the times, and challenges, that we face are different from the ones that Mr. Willson wrote about back in 1974.

Thanks again for coming tonight. And now let's turn to your questions.