

WSJ Print Edition

The central bank should focus on its dual mandate and not try to solve all the economy's problems.

What the Federal Reserve Can Do to Help Itself

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President Trump's threat to nominate a new Federal Reserve chairman who will lower interest rates is misguided. History suggests that the economy and financial markets perform best when the Fed prioritizes price stability, and performance suffers when other goals take precedence. A central bank operating independently generates the best outcomes. Not

All presidents want lower rates, but controlling rates without regard to how they may affect economic conditions and inflation has proved costly. President Richard Nixon collaborated with Chairman Arthur Burns to impose wage and price controls in 1971 and then had Burns pump up monetary policy in 1972 to enhance his re-election bid. Economic chaos resulted.

President Lyndon B. Johnson bullied Chairman William McChesney Martin not to raise rates in 1965, which helped to initiate the Great Inflation that lasted through 1982. President Harry Truman extended the Treasury's request that the Fed peg interest rates during World War II and forced it to maintain low interest rates during the postwar economic boom, and inflation spiked. Argentina, Turkey and other international experiments with government control of central banks have been worse.

Now isn't the time to politicize the Fed or browbeat it to focus on lowering interest rates. Lower rates can't create permanent jobs or offset the negative distorting effects of harmful tariff or immigration policies. Challenging the Fed's independence risks undercutting its credibility, which underpins the dollar's role as the world's reserve currency. Those priorities supersede errant attempts to pump up the economy.

Unfortunately, the larger risk to the Fed's independence is the mounting government debt stemming from decades of bipartisan fiscal irresponsibility. The compounding of inflation-indexed entitlement programs has overwhelmed the political appetite to tax. Mr. Trump was too lax in extending tax cuts in the 2017 Act and missed an opportunity to cut future retirement program spending. Blaming Fed Chair Jerome Powell's high rates as costing a lot of money is a populist plea for monetary accommodation.

This followed President Joe Biden's fiscal profligacy. Roughly a month after enacting his \$1.9 trillion American Rescue Plan in March 2021, Mr. Biden proposed an additional \$3.5 trillion, which included significant deficit spending. Team Biden argued that the Fed would keep rates at zero, so it was prime time to "go big." Fortunately, this over-the-top legislation was blocked by Sen. Joe Manchin (D., W.Va.).

In this troubled environment, the Fed must continue to pursue its dual mandate of low inflation and maximum employment without outside hindrance. Its best response to Mr. Trump should be to re-establish its objectives and incorporate them into its upcoming strategic plan. This will require correcting the flaws in the Fed's 2020 strategic plan and improving communications so that the executive branch, Congress and the public better understand how the Fed achieves its objectives.

The Fed should re-establish symmetry in its inflation and employment mandate, remove its overly complex average flexible inflation targeting and reinstate pre-emptive tightening to manage inflationary expectations. It must pledge to focus on its narrow mandate and not allow its policies to stray into fiscal and credit issues.

The Fed must also acknowledge that its judgment isn't always right, and consider how simple rules may complement and improve its discretionary decision-making approach. Adding a Taylor Rule estimate into the Fed's quarterly summary of economic projections—where Federal Open Market Committee members provide their estimates (the "dot

plot”) for the policy rate needed to meet inflation and economic goals— would be instructive. When the Taylor Rule estimate notably differs from the FOMC members’ estimates, the Fed should take heed.

Other improvements to the summary of economic projections would include more information on the Fed’s balance sheet and conducting an annual risk management exercise in which FOMC members are asked to provide policy-rate estimates for different economic and inflation scenarios. Explaining more rigorously its rationale for changing policy rates would help the White House and Congress better understand the Fed’s monetary policy deliberations.

Fiscal policymakers and the Fed must have a strategy that is in the best interest of the current and future generations. Fiscal responsibility and deficit reduction are needed, and they can be accomplished by a serious bipartisan effort that puts the national interest above nasty politics. That effort is needed to prevent runaway debt and the fiscal dominance of the Fed.

The Fed can’t rely on its independence and be content with small adjustments to its strategic plan. It must make significant progress toward a robust, systematic low-inflation strategy that is consistent with sustainable growth and maximum employment.

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