KOCHERLAKOTA SAYS FED SHOULD MAKE PUBLIC CONTINGENCY PLAN

The U.S. central bank should develop and make public a contingency plan that would explain how it would react to developments in the economy, says Federal Reserve Bank of Minneapolis President Narayana Kocherlakota. A contingency plan such as this one set by the policy-setting Federal Open Market Committee would ''provide clear guidance on how it will respond to a variety of relevant scenarios,'' Kocherlakota has said today in a speech in Sioux Falls, South Dakota. Kocherlakota has said that this contingency plan would reduce uncertainty about the Fed's actions among consumers and companies, which Kockerlakota said has reduced incentives to spend and hire. Kocherlakota has also said that this would enhance the central bank's credibility and transparency. His comments have extended a discussion among members of the FOMC about how to better explain their forecasts and policies to the public. Fed Chairman Ben S. Bernanke said last week in a press conference, that options include clarifying the central bank's long-term inflation goal, publishing the likely path of interest rates, and tying the Fed's pledge to hold rates low to specific levels of employment and inflation. Which is also a strategy espoused by Chicago Fed President Charles Evans. At its Nov 1-2 meeting, the Fed reached no decision to adopt a new communication strategy and they didn't decide on any additional programs to combat an unemployment rate that has stayed near 9 percent or higher for 31 months. After joining Dallas Fed President Richard Fisher and Philadelphia's Charles Plosser in dissenting from the previous two statements announcing new stimulus measures, Kocherlakota supported this month's policy statement. In a separate speech today in Philadelphia, Plosser said that the Fed should adopt a 2 percent inflation target to increase the accountability of policy makers and improve economic stability. While lacking a formal taget, the Fed is currently aiming to keep the inflation at about 2 percent. ''Marking such a clear and explicit statement should give the public confidence that the Fed's commitment to its price stability mandate is a credible one,'' says Plosser. ''Being explicit about our inflation objective would help anchor expectations and reduce uncertainty about future policy steps.'' The central bank has ''tools remaining'' to lower borrowing cost says Kocherlakota. He says that, as well as ''extend its prediction for how long it will keep its target short-term interest rate exceptionally low,'' it could buy more Treasury securities or housing debt. ''However, the FOMC should do more than simply decide at each meeting whether or not to buy more assets or to keep interest rates low for longer,'' says Kocherlakota. ''Suppose hypothetically that core inflation, and the outlook for core inflation, has risen to 3 percent by the end of 2013, while unemployment has fallen to between 8 percent and 8.5 percent,'' he said. ''A public contingency plan would allow the public to know what the committee intends to do in that eventuality.''