

# *Fed Official Warns of Risk From Hasty Rate Increase*

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WASHINGTON — Narayana Kocherlakota, president of the Federal Reserve Bank of Minneapolis, said on Friday that the Fed's latest steps toward raising interest rates increased an "unacceptable" risk that the economy would fall into an enduring period of low inflation.

Mr. Kocherlakota, who voted against the measures that the central bank announced on Wednesday, said in an interview that the Fed was taking an unnecessary gamble. He reiterated his view that the Fed should declare an intention to keep the crucial interest rate lever it controls near zero until the inflation outlook improves.

But he said that he saw little chance of winning the debate and that he hoped he would not be vindicated by events.

"You know, what I hope does not happen is that the evolution of the data makes them come around," Mr. Kocherlakota said. "I hope they're proven right. I think there's a risk here being taken by the committee, and for the good of the economy, I hope it turns out well for them."

While low inflation may sound like a good thing, Fed officials generally agree that annual inflation of about 2 percent has important economic benefits.

It strengthens the Fed's ability to counteract economic downturns by providing room to reduce borrowing costs when needed. It also helps the economy to rebound by allowing nominal cuts in wages and prices, which are easier to impose than real cuts.

The Fed indicated on Wednesday, after a two-day meeting of its policy-making committee, that it remained likely to start raising interest rates around the middle of next year, even though inflation has been below the Fed's 2 percent annual target for years and Fed officials predict prices will rise even more slowly next year.

The Fed's plans are based on its expectation that inflation will begin to rebound in 2016 as the job market tightens and the economy continues to advance at a healthy pace. John Williams, president of the Federal Reserve Bank of San Francisco and a member of the majority led by Janet L. Yellen, the fed chairwoman, said in an interview on Friday with Bloomberg Radio that there was "no question" that the Fed would start raising rates before inflation reached 2 percent.

Two other officials also voted against the Fed's decision, although for the opposite reason. They argued that the Fed was not moving fast enough. Richard W. Fisher, president of the Federal Reserve Bank of Dallas, and Charles I. Plosser, president of the Federal Reserve Bank of Philadelphia, both expressed concern that the Fed was underestimating the strength of the economic recovery and that it would need to raise rates more quickly.

"While the communication indicated that the forward guidance had not changed, the U.S. economy continues to improve more rapidly than expected," Mr. Plosser said in a statement on Friday. Describing recent economic data, he added, "These are not the characteristics of an economy in need of extraordinary monetary accommodation."

Mr. Fisher did not elaborate on his reasons for dissent on Friday, after the Fed ended a post-meeting quiet period.

It is the first time since 2011 that three officials have dissented from a decision of the Federal Open Market Committee, which makes Fed policy, at the same time. As it happens, the same officials dissented on the last occasion, although back in 2011, all three wanted the Fed to retreat from its stimulus campaign. Mr. Kocherlakota has since changed his mind.

Such a high level of dissent is unusual — before 2011, it last happened in 1992 — because the Fed aims to set policy by consensus. It tries to shape expectations about its future conduct, and dissents tend to undermine confidence that the Fed will follow through.

Wednesday was Mr. Kocherlakota's last vote on monetary policy — the presidents of most reserve banks vote every third year, and Mr. Kocherlakota said this month that he would step down in February 2016. He used the moment to again sound an alarm.

“In my assessment, the FOMC's failure to respond to weak inflation runs the risk of creating a harmful downward slide in inflation and longer-term inflation expectations of the kind that we have seen in Japan and Europe,” he said in a statement. “I see this risk to the credibility of the inflation target as unacceptable.”

Mr. Kocherlakota noted that inflation had run below the Fed's target in each of the last 30 months, that the Fed's staff forecast inflation would remain below the Fed's target for the next few years and that some measures of investors' inflation expectations had fallen sharply.

“We chose 2 percent for a good reason, and that was to provide enough capacity to help buffer the economy against shocks,” Mr. Kocherlakota said. “If the inflation rate gets stuck at a low level, then we lose our ability to buffer against shocks.”

And as Japan has discovered, once inflation sags, it can be hard to revive.

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