Changing Governance Practices Seem to Have Reduced the Diversity of Views at the Federal Reserve

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Later this year the Federal Reserve will begin their promised review of their monetary policy strategy. The last review, conducted in 2019 and 2020, resulted in a substantial revision of the original 2012 monetary policy strategy statement. The revisions were motivated in large part by the perceived shortcomings in the conduct of policy under the earlier framework. The surge in inflation in 2021 and early 2022 will no doubt be front and center in their upcoming review. The Federal Reserve System's delayed response to that surge is now widely regarded as having been an error.[1]

Many factors have been cited as contributing to the Fed's disappointing performance—such as the effects of the revised framework document adopted in August 2020, the strong forward guidance provided in September 2020, the commitment to not begin raising rates until the end of assets purchase, and the overestimation of labor market slack in 2021. The considerations will no doubt feature prominently in the Fed's strategic review. I would argue that, alongside these contributing factors, the Fed should seriously consider whether their decision making would have benefitted by more robust engagement with diverse perspectives. The scarcity of dissenting votes at Federal Open Market Committee meetings and the increasing homogeneity of public statements by FOMC participants during this episode provides strong evidence of a decline in the diversity of viewpoints among Fed decision makers.

This essay is drawn from remarks given at an October 2023 Mercatus Center conference honoring "The Legacy of Bennett McCallum and Lessons for Monetary Policy Today," during a panel on the subject "What Is the Future of Federal Reserve Governance?" My full remarks were published in January 2024 as a [Mercatus Center Policy Brief] and reprinted in *Central Banking*. I am grateful to Esther George, Huberto Ennis, Al Broaddus, and Tracy Miller for comments on earlier drafts.

[1] For example, in a 2023 Brookings Institution conference paper, authors Gauti Eggertsson and Don Kohn argue that earlier recognition by the Fed of the seriousness of the inflation surge and earlier response to the surge likely would have dampened demand sooner, lessened the increase in inflation, and enabled a more gradual tightening of policy. Gauti B. Eggertsson and Donald Kohn, "The Inflation Surge of the 2020s: The Role of Monetary Policy" (Working Paper 87, Hutchins Center on Fiscal and Monetary Policy at Brookings, August 2023), 3. See also Athanasios Orphanides, "Enhancing Resilience with Natural Growth Targeting," Working Paper Series No. 200 (Goethe University Frankfurt: Institute for Monetary and Financial Stability, February 2024), and Mickey D. Levy and Charles I. Plosser, "The Murky Future of Monetary Policy" (Shadow Open Market Committee, New York, NY, October 1, 2020).

Two apparent shifts in Federal Reserve governance practices may have contributed to the decline in viewpoint diversity: The Board of Governors of the Federal Reserve System has played a more active role in the search for Reserve Bank presidents, and the norms around public communications by FOMC participants seem to have shifted. In both cases, the evolution of governance practice may have been motivated by a desire to reduce the political costs to the Board of public expression of alternative perspectives. The Board should consider the possibility that such costs are worth bearing for the sake of more robust and resilient monetary policy decision making.[2]

Evolving Governance at the Federal Reserve

In the final paragraph of their 2023 Brookings Institution conference paper, Gauti Eggertsson and Don Kohn note that despite challenges facing Fed policy making in 2021 and 2022, "no FOMC voters dissented between September 2020 and June 2022, raising questions about whether Committee discussions and decisions were being sufficiently challenged by diverse viewpoints."[3] Not only were formal dissenting votes largely absent during a period of widely divergent views among economists outside of the Fed, but few FOMC members expressed differing views in their public speeches and interviews. That there was so little public display of divergent views from Committee participants is striking.

The paucity of evidence of diverse views within the FOMC in recent years continues a longer-run trend: See Figure 1. Dissents by members of the Board of Governors virtually disappeared in the late 1990s.[4] Although dissents by Reserve Bank presidents also fell after the 1990s, such dissents became frequent again during and after the 2007-2009 recession, which is understandable given the Fed's innovative and controversial credit market intervention. But since then, the frequency of per-meeting dissents has been declining. Under Chair Bernanke there were 0.73 dissents per meeting overall and 1.03 dissents per meeting from 2010 through 2013, his last four-year term. Dissents fell slightly to 0.70 per meeting under Chair Yellen, but have plummeted to 0.31 per meeting under Chair Powell. It's also fair to say that public expressions of alternative policy perspectives by Committee participants have declined since 2010. And Mickey Levy has noted a surprising lack of dispersion in the published economic projections of Committee participants.[5]

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[2] Andrew T. Levin and Christina Parajon Skinner provide a thorough description of the limitations of the governance and accountability mechanisms around the Federal Reserve, along with proposals for reform: Andrew T. Levin and Christina Parajon Skinner, "Central Bank Undersight: Assessing the Fed's Accountability to Congress," 2023.

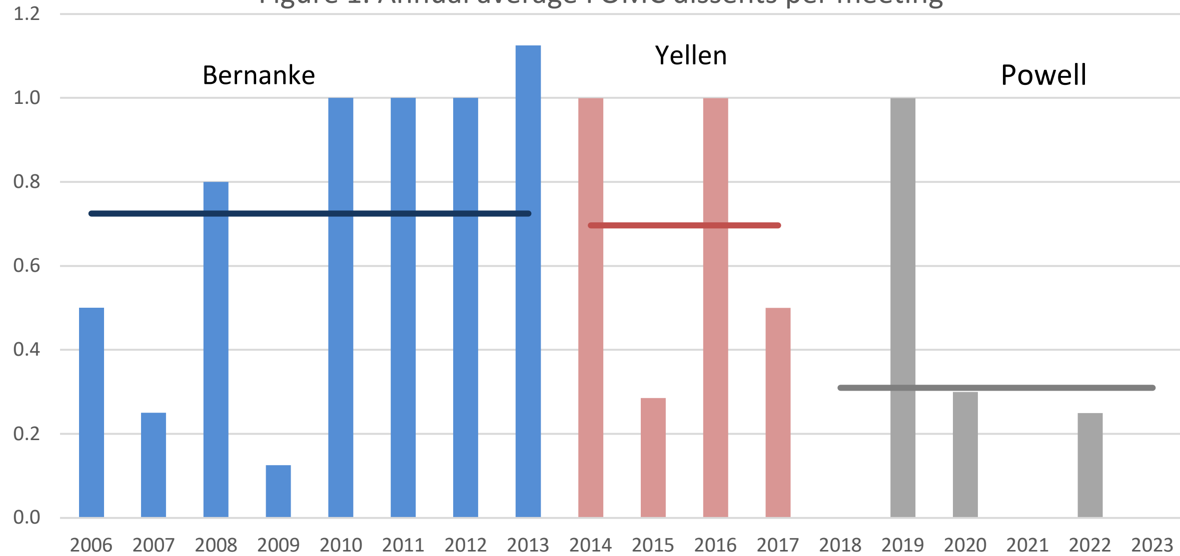
[3] Eggertsson and Kohn, "The Inflation Surge of the 2020s: The Role of Monetary Policy," 35. Actually, Jim Bullard, then president of the Federal Reserve Bank of St. Louis and a voting member of the FOMC, dissented on March 16, 2022, the first meeting at which the FOMC raised interest rates following the COVID-19 pandemic, preferring to raise the target for the federal funds rate by 50 basis points rather than 25.

[4] Daniel L. Thornton and David C. Wheelock, "Making Sense of Dissents: A History of FOMC Dissents," *Federal Reserve Bank of St. Louis Review* 96, no. 3 (2014). There have been just two dissents by governors since 1995 and just four since 1990, whereas there were 63 dissents by governors from 1980 to 1989.

[5] Mickey D. Levy, "The Fed: Bad Forecasts and Misguided Monetary Policy," in *Getting Monetary Policy Back on Track*, ed. Michael D. Bordo, John H. Cochrane, and John B. Taylor (Stanford, California: Hoover Institution, 2024), 266.

I offer two conjectures about what might explain the decline in the apparent diversity of views. Both have to do with the Fed's governance practices, broadly construed, and both deserve careful reconsideration by the Fed's leadership in the wake of this episode. My first conjecture is that a change in the Board of Governors' role in the Reserve Bank presidential searches since 2010 has resulted in a change in the profile of Reserve Bank presidents and a reduction in the diversity of views around the table.

Figure 1. Annual average FOMC dissents per meeting



Reserve Bank presidents are appointed by nonbanker directors of their respective Reserve Banks "with the approval of the Board of Governors," according to the Federal Reserve Act.[6] In the 2000s, the Board played a relatively hands-off role until the end of the search process, after the Reserve Bank had settled on its desired candidate. The governor serving as chair of the Bank Affairs Committee (a group of governors responsible for overseeing Reserve Bank operations) would generally be the point of contact with the Reserve Bank's board. The head of the Reserve Bank search committee, typically the board chair, would check in periodically by phone and provide general progress reports. After the Reserve Bank had decided on its presidential candidate, the Board of Governors would be informed, allowing it to weigh in before the candidate's name was formally voted on by the Reserve Bank and submitted to the Board for approval. On occasion, the Board would then let the Reserve Bank know that its chosen candidate would likely be rejected and would advise the Reserve Bank to reconsider its choice. In some cases, the Reserve Bank would follow the Board's recommendation and select another candidate, but in other cases there would be a stand off between the Board of Governors and the Reserve Bank until one of them backed down. However, the Board's involvement during the

[6] Specifically, they are to be appointed by the Class B and Class C directors. Class B directors are nonbankers elected by the member banks, and Class C directors are appointed by the Board of Governors.

actual search process, before the Reserve Bank's initial candidate decision, was generally fairly limited.

In recent years, the Board has been much more involved in the early stages of presidential searches. There are frequent scheduled calls between the search committee head and the chair of the Bank Affairs Committee, lists of prospects are shared with and vetted by the Board early on, and names of prospective candidates are suggested to the Reserve Bank. In essence, the Board's role appears to have shifted from final-stage review and approval, as suggested by the language of the Federal Reserve Act, to co-management of the presidential search process.[7] This more extensive early involvement enables the Board to more directly shape the selection process and steer the Reserve Bank's choice toward candidates that the Board finds more suitable. My conjecture is that the Board has used its more active involvement in presidential searches to steer Reserve Bank boards toward candidates with a greater affinity for the Board's policy views and a disinclination to diverge publicly from those views. In fact, achieving that result may have been the Board's motivation for more active involvement in presidential searches.

One indicator that aligns with this conjecture is the noticeable shift that has occurred in the composition of the presidents. In 2009, just over half of the presidents had records of multiple academic journal publications in monetary economics and macroeconomics. All but two of such presidents had retired or stepped down by late 2021, and no new presidents with such characteristics have been named since the appointment of John Williams as president of the Federal Reserve Bank of San Francisco in 2011.[8] Such an active research background in disciplines closely related to monetary policy plausibly provides an FOMC participant with more confidence in coming to divergent assessments of policy issues and with a greater willingness to question the majority's view in public. Moreover, a background in the theoretical grounding of macroeconomic analysis is especially useful at sharp turning points, when empirics alone are less helpful and theoretical reasoning can play a critical role.

I am not asserting that an academic research career in monetary economics is a prerequisite for arriving at divergent assessments about monetary policy and voting or speaking out accordingly. There are certainly many counterexamples; Esther George and Tom Hoenig, both former presidents of the Federal Reserve Bank of Kansas City, would be prominent among them, along with Tom Melzer of the Federal Reserve Bank of St. Louis. I am just highlighting a readily observable factor that might relate to a Reserve Bank president's propensity to dissent. More subjective and less readily observed factors are undoubtedly relevant as well. For example, presidents may differ in their approach to using their Reserve Bank's research department,

[7] Christopher Condon, "Fed Documents Show Powell's Hand in Richmond President Search," *Bloomberg*, July 16, 2018. Records obtained by Bloomberg News under a Freedom of Information Act request "show that in 2017 then–Fed Governor Jerome Powell kept up a running discussion by phone and email with officials at the Richmond Fed" during their 10-month search for a president, including sharing names of potential candidates and providing feedback on names compiled by the Richmond Board and its search firm.
[8] Williams began serving as president of the Federal Reserve Bank of San Francisco in March 2011 and then began serving as president of the Federal Reserve Bank of New York in June 2018.

which often serves as a source of independent thinking. And presidents may have different philosophies about the role of public dissent at the FOMC. My conjecture is that, on an array of dimensions, a noticeable shift in the composition of the presidents has taken place over the past decade or so as a result of the deeper pre-appointment role the Board now plays in presidential selections.

There is an important tradeoff here that Fed leaders would do well to recognize. The presumption underlying deliberative policy bodies is that the quality of decision-making is strengthened when diverse perspectives are voiced and given serious consideration. This concept is, of course, a key rationale behind the movement to enhance diversity and inclusion in organizations; the idea is that greater ethnic and racial diversity expands the diversity of intellectual perspectives brought to bear on collective decision-making. And the value of diverse perspectives was a strong driving force behind the adoption of a federated structure at the origin of the Federal Reserve System, whose founders saw the geographic diversity provided by twelve dispersed Reserve Banks as adding a vital intellectual breadth to the Fed's deliberations. This feature survived the amendments made to the Federal Reserve System by the Banking Act of 1935, which established the FOMC and increased the power of the Board of Governors.

Evolving Communication Norms

My second conjecture is that there has been a shift in committee norms regarding FOMC participants publicly airing divergent views. Under former Fed Chairman Alan Greenspan, the sharing of independent views, especially about the monetary policy outlook, was rare. As chair, Greenspan served as virtually the sole conduit for what FOMC messaging took place.

Former Fed Chairman Ben Bernanke, in contrast, promoted transparency and open communication. Under Bernanke, Reserve Bank presidents enjoyed more latitude to articulate their own framework and views. Over time, this openness led to greater expression of individual policy views by FOMC participants both inside and outside FOMC meetings. I would argue that, consistent with Bernanke's expectations, this greater openness aided public understanding of the Fed and its mission. The firestorm of criticism that arose in the wake of the Fed's interventions during and after the 2007-2009 financial crisis, however, made divergent views politically inconvenient for the Board, because it allowed critical members of US Congress and the public to cite the alternative views of Fed insiders.

Some important elements of Bernanke's "glasnost" remain, such as post-meeting press conferences and the quarterly Summary of Economic Projections. But in the past few years, the Fed appears to be returning to a less open approach to public communications. At times, the FOMC seems to be behaving more like a corporate board, keeping dissenting views internal and hewing to the "house view" externally. This norm contrasts with that of deliberative public policy bodies, such as the U.S. Securities and Exchange Commission and the board of the Federal Deposit Insurance Corporation, whose members feel accountable for articulating their views to the public. One can see why the corporate model would be attractive to Board leadership, however, given the intense scrutiny of the Fed since 2008. The chair gets tighter control over messaging to Congress and is less often forced to answer questions about alternative views within the Fed, thus making external political relations easier to manage.

Remarks on this subject by the current Federal Reserve Chair, Jerome Powell, provide some insight into the thinking that may now be shaping FOMC communication norms. At a Brookings Institution conference in November 2016 titled "Understanding Fedspeak," Powell, then a member of the Board of Governors under Chair Yellen, provided "A View from the Fed." In a section of that speech titled "Cacophony," he discussed the airing of divergent views by FOMC participants.

> In my view, the public expression of our diverse views helps sustain public support for the Federal Reserve as a public institution. Those members of the public who disagree with our policy should know that their concerns are given voice in our deliberations. But there is a tradeoff here that needs to be managed: On the one hand, the effectiveness of policy is thought to depend on the public's understanding of the Committee's consensus. On the other hand, the expression of diverse views may sometimes make it difficult for the public to see that consensus.[9]

This last sentence is a bit confusing. If the full range of FOMC participants' views are being shared, including the views of the Chair, then presumably the public can see just how much of a consensus there is. Powell may have in mind that the expression of diverse views reduces attention to other, "consensus," views, such as the views of the Chair.[10]

Powell, referencing a paper earlier in the conference by Jon Faust, a Board economist, goes on to denigrate the motives of participants speaking in public and to point out that the views of the Chair are the more relevant than others.

> Jon sees this public discussion about policy as mainly a form of negotiation. In my view, motivations are simpler and more obvious. Many of us enjoy getting out of the office to speak to outside groups. We appear to enjoy talking to print journalists, and some of us like going on television. With the proliferation of media of all kinds, there is a need for content, and we have been willing suppliers. In my view, these public appearances are mostly not about gaining leverage in a negotiation. There is a single FOMC participant who has most of the leverage in our policy discussions. Observers would be well advised to listen carefully to what she says.
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> I strongly agree with Jon that it is wise not to read too much about the path of policy into all of this communication. FOMC participants other than the Chair speak only for

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[9] Jerome H. Powell, "A View from the Fed" ("Understanding Fedspeak," an event cosponsored by the Hutchins Center on Fiscal and Monetary Policy at the Brookings Institution and the Center for Financial Economics at Johns Hopkins University, Washington, D. C., November 30, 2016), 12.

[10] The Merriam-Webster dictionary defines consensus as: "1a: general agreement: unanimity, 1b: the judgment of most of those concerned, 2: group solidarity in sentiment and belief". Divergent views see inconsistent with meanings 1a and 2.

> themselves and customarily make that clear at the beginning of their remarks. Their commentary is not intended to express the consensus or to predict its evolution.
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> As Jon notes, during the Greenspan era, there was very little discussion of the likely path for the policy rate by FOMC participants, including the Chairman. The proliferation of forward policy guidance during the crisis utterly broke that equilibrium. Many of us seem to be trained to a new habit, which is to offer one's views about the near-term path for policy, typically at the end of a speech on the outlook. While such communication can serve a useful purpose, I have come around to the view that focusing too much on the precise timing of policy moves may be adding to confusion and frustration about our communications. I am trying to avoid this problem in my own remarks.[11]

One can see here a communication philosophy that would privilege public expression of the views of the Committee Chair ("the single FOMC participant who has most of the leverage"). Expressions of alternative views, to the extent they diverge from those of the Chair, add "confusion and frustration." One can see how this approach could have led the current chair to promote an expectation that participants emphasize the Committee "consensus" in public communication and limit the expression of their own views.

Powell clearly recognizes a value to public airing of alternative views that are present within the Committee. As he puts it, it is worthwhile that the public "know that their concerns are given voice in our deliberations." But beyond this simple affirmation of representation, there is a broader benefit to the public in knowing that a robust range of views are being considered, even views with which they disagree. The Fed should want to demonstrate that, for decisions as challenging as monetary policy, deliberations are thorough and rigorous. And in the event that the Fed's assessments shift—for example, abandoning the view in 2021 that inflation is "transitory"— having aired differing perspectives ahead of time will better prepare public understanding and dampen the appearance of capriciousness. The Fed's credibility will be enhanced if changes in its assessments are well understood. Moreover, an organizational norm of tolerating public articulation of alternative views can enhance the incentive of other participants, including the chair, to take alternative views seriously when expressed internally, since external expression of those views may spark public queries.

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As they reflect on the inflation surge of 2021–2022, and on the Fed's response, Fed leaders would do well to consider, as Eggertsson and Kohn suggest, "whether Committee discussions and decisions were being sufficiently challenged by diverse viewpoints."[12] The recent evolution of governance practices that I have described may have played a significant role in reducing the diversity of viewpoints that were given serious internal consideration in 2021–2022. Whatever

[11] Powell, "A View from the Fed," 12–13.
[12] Eggertsson and Kohn, "The Inflation Surge of the 2020s: The Role of Monetary Policy," 35.

other objectives those practices may have achieved, they may have contributed to notably disappointing monetary policy outcomes.