WASHINGTON, DC- Deflation fears that have taken root are unfounded and misguided, according to the Shadow Open Market Committee (SOMC) at its semiannual meeting today.

The SOMC argued that while inflation is modest, deflation is a remote possibility. The committee noted that deflation is not necessarily destabilizing to the economy and even if it were to unfold, the Federal Reserve is capable of expanding the money supply to accelerate normal demand.

“The lack of systematic guidelines for the conduct of monetary policy continues to contribute uncertainty to the economic environment,” the SOMC stated.

The SOMC urged the Federal Reserve to adopt explicit objectives for monetary policy and guidelines that would make policy more transparent. Adopting some form of inflation targeting similar to some 15 other nations’ central banks would provide many positive contributions to monetary policy.

The SOMC noted that inflation targeting would provide equally beneficial guidelines in situations of deflation as well as inflation. For example, the SOMC explained, inflation targeting in Japan would contribute to eradicating its deflation.

The SOMC described two monetary policy indicators, the so-called Taylor Rule and the McCallum Rule, proposed by SOMC member Bennett McCallum. According to the latter rule, recent growth of the monetary base is consistent with a 2 percent inflation target, which the SOMC deemed appropriate.

Monetary policy indicators are carried on the SOMC website: http://www.somc.rochester.edu

The SOMC maintained its advocacy of tax reforms that “lower marginal tax rates and reduce the excessive taxation of capital.” It expressed concern that the current fiscal policy debate was dominated by deficit fears and arbitrary budget deficit projection targets. According to the SOMC, the focus on budget deficits is misleading and draws attention away from tax reforms that would enhance economic growth and create jobs.

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Shadow Open Market Committee Web Site:
http://www.somc.rochester.edu