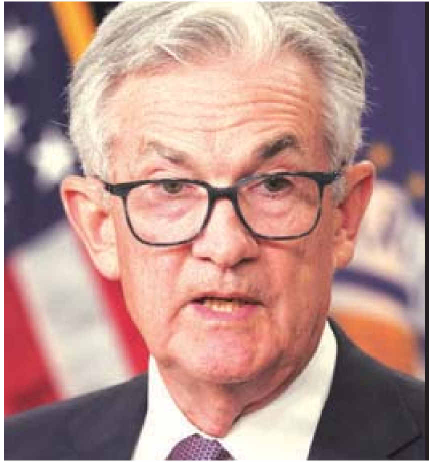
Powell's message: Inflation fight may cause recession

ASSOCIATED PRESS
22 September

The Federal Reserve delivered its bluntest reckoning on Wednesday of what it will take to finally tame painfully high inflation: Slower growth, higher unemployment and potentially a recession.

Speaking at a news conference, Chair Jerome Powell acknowledged what many economists have been saying for months: That the Fed's goal of engineering a "soft landing" — in which it would manage to slow growth enough to curb inflation but not so much as to cause a recession — looks increasingly unlikely.



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JEROME POWELL,
Chair, US Federal Reserve

"The chances of a soft landing," Powell said, "are likely to diminish" as the Fed steadily raises borrowing costs to slow the worst streak of inflation in four decades.

"No one knows whether this process will lead to a recession or, if so, how significant that recession would be." Before the Fed's policymakers would consider halting their rate hikes, he said, they would have to see continued slow growth, a "modest" increase in unemployment and "clear evidence" that inflation is moving back down to their 2 per cent target.

"We have got to get inflation behind us," Powell said. "I wish there were a painless way to do that. There isn't." Powell's remarks followed another substantial three-quarters of a point rate hike — its third straight — by the Fed's policymaking committee.

Its latest action brought the Fed's key short-term rate, which affects many consumer and business loans, to 3 per cent to 3.25 per cent. That's its highest level since early 2008.

Falling gas prices have slightly lowered headline inflation, which was a still-painful 8.3 per cent in August compared with a year earlier. Those declining prices at the gas pump might have contributed to a recent rise in President Joe Biden's public approval ratings, which Democrats hope will boost their prospects in the November midterm elections.

On Wednesday, the Fed officials also forecast more jumbo-size hikes to come, raising their benchmark rate to roughly 4.4 per cent by year's end — a full point higher than they had envisioned as recently as June.

And they expect to raise the rate again next year, to about 4.6 per cent. That would be the highest level since 2007.

By raising borrowing rates, the Fed makes it costlier to take out a mortgage or an auto or business loan. Consumers and businesses then presumably borrow and spend less, cooling the economy and slowing inflation.

In their quarterly economic forecasts, the Fed's policymakers also projected that economic growth will stay weak for the next few years, with unemployment rising to 4.4 per cent by the end of 2023, up from its current level of 3.7 per cent.

Historically, economists say, any time unemployment has risen by a half-point over several months, a recession has always followed.