Powell Backs Quarter-Point Rate Rise in March Despite Ukraine War Effects

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The Federal Reserve is prepared to push ahead with a "series" of interest rate increases from March, despite a highly uncertain economic outlook as a result of Russia's invasion of Ukraine, Jay Powell told US lawmakers on Wednesday.

The Fed chair confirmed his support for a quarter-point rate rise at the central bank's March meeting as he laid out the case for tightening monetary policy amid heightened geopolitical tensions, in testimony delivered to the House Financial Services Committee.

Powell said he expects a "series" of interest rate increases this year, and also hinted that he could support raising rates by larger increments later on if inflation fails to moderate sufficiently.

"I'm inclined to propose and support a 25bp rate hike," he said. "The bottom line is that we will proceed, but we will proceed carefully as we learn more about the implications of the Ukraine war for the economy."

He said separately: "To the extent inflation comes in higher or is more persistent . . . then we would be prepared to move more aggressively by raising the federal funds rate by more than 25bp" at one or more meetings.

In justifying his thinking, Powell highlighted the broad-based employment gains that have accrued over the past six months in what has been an "extremely tight" labour market that has led to rapidly rising wages. He also called attention to consumer price increases "spreading to a broader range of goods and services" that have driven inflation up to the fastest pace in 40 years.

The Fed still expects inflation to moderate this year as severe supply-demand mismatches subside, but Powell said he is "humble" about being able to forecast when that may happen.

"Inflation is indisputably too high," the chair said, adding that the phenomenon is not just strong across the goods sector, but also "too high" in services. "We are using our tools to bring inflation back down to levels of price stability, and we will accomplish that task."

He also pushed back on the notion that a series of interest rate increases would imperil the economy, even as he floated the idea of eventually raising rates to a level that begins to constrain activity.

“I think it’s more likely than not that we can achieve what we call a soft landing,” he said.

Powell’s positive assessment of the economy and pledge to act more forcefully to counter mounting price pressures, come despite a sharp escalation in Russia’s attacks on Ukraine, with the Kremlin stepping up bombardments on the country’s biggest cities.

The war in Ukraine has clouded the growth outlook, but is also forecast to exacerbate inflation — energy prices have surged with Brent crude climbing to its highest level in eight years, at roughly $111 a barrel — and could potentially force the Fed to be more aggressive later this year than markets currently anticipate.

Powell said the near-term economic implications from the invasion and the sanctions levied by Washington and its western allies — which US president Joe Biden called “powerful” during his State of the Union address on Tuesday — remain “highly uncertain”, but vowed to monitor the situation closely.

“Making appropriate monetary policy in this environment requires a recognition that the economy evolves in unexpected ways,” Powell said. “We will need to be nimble in responding to incoming data and the evolving outlook.”

Markets are pricing in just over five quarter-point interest rate increases during the course of 2022 compared with the six that were pencilled in before Russia’s invasion of Ukraine.

Given current expectations and recent market gyrations, Powell said the rate increases “have already happened in effect and we have to ratify them”.

Alongside plans to raise rates, the Fed will also begin scaling back its $9tn balance sheet. While no details have yet been provided about when that process may begin and at what pace, Powell on Wednesday suggested a roughly three-year timeline to shrink it to levels where “it needs to be”.