Treasury Secretary Yellen warns interest rates may need to rise

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US Treasury Secretary Janet Yellen has said the Federal Reserve may have to lift interest rates in order to head off inflation in the US economy.

She made the comments in a pre-recorded statement for an event hosted by the *Atlantic* magazine as growing concerns have been raised over whether Biden's spending plans will lead to an increase in inflationary pressures.

"It may be that interest rates will have to rise somewhat to make sure that our economy doesn't overheat, even though the additional spending is relatively small relative to the size of the economy," Yellen said.

"So it could cause some very moderate increase in interest rates to get that reallocation. But these are investments our economy needs to be competitive and to be productive."

Coming from a former Fed chief, Yellen's comments were something of a departure from previous practice in which Treasury secretaries do not comment on Fed policies and the Fed refrains from commenting on the policies of the administration.

Aware of the concerns in financial markets about the prospect of an interest rate rise, Yellen appeared to backtrack somewhat from her remarks in later comments in an interview at a CEO Council Summit held by the *Wall Street Journal*.

In that forum, she said a lift in interest rates by the Fed was "not something I'm predicting or recommending."

"I don't think there's going to be an inflationary problem, but if there is, the Fed can be counted on to address it," she stated.

Asked about the position of the Biden administration on Yellen's assessment, White House press secretary Jen Psaki told reporters the president agreed with the Treasury Secretary and the White House was keeping a close watch on prices.

"We also take inflationary risks incredibly seriously, and our economic experts have conveyed that they think this would be temporary and that the benefits far outweigh the concern," Psaki said.

Inflation concerns have been voiced by former Treasury Secretary Lawrence Summers who has said the Biden administration's spending measures risk setting off the kind of price rises seen in the 1970s.

There is a degree of nervousness in financial markets that if inflation begins to rise, the Fed may be forced to increase rates. This would have an immediate adverse impact of Wall Street where money has been raked in hand over fist because of the massive support provided by the Fed—low rates combined with the injection of trillions of dollars via financial asset purchases since the market freeze of March 2020.

Signs of that nervousness were evident yesterday when there was a fall in US technology stocks which had their worst daily performance for nearly two months. The tech-heavy NASDAQ index dropped by 1.9 percent while the S&P index dropped by 0.7 percent.

The *Financial Times* reported that "traders and investors said they there increasingly unnerved that higher inflation was beginning to emerge"—a fear underscored by Yellen's remarks.

The Fed has largely dismissed concerns that inflation is about to take off and has maintained that recent price rises are "transitory." Fed chair Powell has insisted that ultra-low rates will be retained for a "long time." In other words, the flow of money that has sent markets to record highs will continue.

But this inflow of money has led to an "everything rally" including in significant industrial commodities.

The price of key industrial commodities, including iron ore, palladium, used to limit harmful emission from cars, and timber have reached all time records.

Copper, one of most important industrial metals, has reached its highest price level in a decade. A commodity price index compiled by Bloomberg is at its highest level in a decade.

One of the fears in the ruling class, though this is rarely raised in financial commentary, is that a rise in inflation will fuel the development of the class struggle as workers press for higher pay in an effort to overcome the wage suppression extending back over decades and the impact of the COVID-19 pandemic.

Under what were previously regarded as "normal" conditions, the Fed would start to tighten monetary policy, not least to suppress wage demands.

But now it is trapped within a framework its own making. The financial markets have now become so dependent on the inflow of money from the central bank that even the smallest move to reduce this flow can set off a market crisis.

In a comment published in the *Financial Times*, financial analyst Mohamed El-Erian warned that "indications of market froth are multiplying in an 'everything rally'" and more companies were warning about rising input costs "with some signalling that this will be passed on to prices."

But, he continued, given its operational framework, adopted last December in which it said it would not consider a tightening of monetary policy until price rises were consistently around or above 2 percent, the Fed had "no operational choice" but to stick to its narrative that the present price increases are "transitory."

El-Erian warned that froth and "excessive risk taking in markets," of which there is increasing evidence, such as the rise of margin debt for investors to record highs, would lead to an "upward migration in both actual and expected inflation."

This could result in a situation where "ultimately, the Fed may be forced to slam on the monetary policy brakes, risking undermining what should be a long-lasting recovery."

In other words, the very policies pursued to bail out the corporations and financial markets as a result of the COVID-19 pandemic could lead to a crash of the financial system and the broader economy.