US Fed chair takes a step towards interest rate cut

Nick Beams
10 July 2024

The chairman of the US Federal Reserve, Jerome Powell, has given his strongest indication yet that the central bank is set to start lowering its interest rate, if not at its next meeting at the end of July, then in September.

In his remarks to the Senate Banking Committee on Tuesday, which were repeated at the House Financial Services Committee yesterday, Powell said the Fed had made "considerable progress" in bringing down price rises but "more good data would strengthen our confidence that inflation is moving sustainably towards 2 percent"—the Fed's target rate.

The clearest indication of a rate cut was Powell's references to a "cooling" of the labour market which has seen the unemployment rate rise to 4.1 percent in June, up from 3.7 percent in December.

Powell said that "elevated inflation is not the only risk we face" and "reducing policy restraints too late or too little could unduly weaken economic activity."

There have been concerns raised that while it is not a major jump, the increase in the jobless rate could accelerate in coming months.

Powell's testimony made clear that from the very outset the central concern of Fed policy has been to clamp down on the wage demands of the working class in response to the highest inflation in four decades.

"We've seen that the labour market has cooled really significantly across so many measures … It's not a source of broad inflationary pressures for the economy now."

In fact, it never was. The source of inflation, and the ongoing price hikes in grocery items and essentials such as gas, was the supply chain crisis set off by the pandemic and then the war in Ukraine, which enabled profit gouging by major global food giants and energy companies.

Powell noted that "nominal wage growth has eased over the past year" and the jobs-to-workers gap was well down from its peak and just a bit above its 2019 level.

While Powell could not publicly acknowledge it, one of the main reasons for the suppression of wage rises has been the crucial role of the trade union bureaucracy in imposing sub-inflationary wage increases on broad sections of the working class.

The union apparatuses have now created the conditions where the Fed feels it is able to move towards interest rate cuts in accordance with the demands of the financial markets.

The main thrust of remarks by Democratic senators, desperately looking for some boost for Biden in the presidential election, or whoever might replace him, was the need to cut rates.

While indicating cuts were on the agenda, Powell refused to give any date as to when they might begin. "I'm not going to be sending any signals about the timing of future actions," he said.

A significant aspect of the hearing was the absence of any questions about the rise in US debt and the problems it could pose for the financial system.

The nearest anyone got was a question from Tennessee Republican Senator Bill Hagerty on the turn by the Treasury to funding the debt at the short end of the debt market—that is, the issuing of bonds of one or two years, as opposed to ten-year bonds.

He said the "excess of short-term debt" seemed to be creating mounting risks for "Treasury market disruption."

Powell did not deal with the issue, saying the Treasury, not the Fed, determined the way in which debt was financed.

The absence of any discussion or questions regarding the growing risks to the US financial system—exemplified by concerns over the functioning of the Treasury market and the failure of three large American banks in March 2023—was highlighted by the focus of many of the remarks by Republican senators on the so-called Basel III Endgame.

This involves the implementation of a new system of bank regulation devised by some 28 central banks in the wake of the 2008 financial crisis. The latest iteration of the measures, after a series of delays, is now set to come into effect in mid-2025 with a three-year adjustment period.

The measures have provoked furious opposition from the major banks because of the increased capital they are required to hold to deal with potential crises.

As an article published last month on the website Investopedia put it, the major banks have attacked the proposals as a “threat to the American economy” and have “amassed an army of lobbyists in Washington DC and poured millions into a campaign to denounce the proposed regulations.

“Lobbies like the Bank Policy Institute have taken to the airwaves and online, warning that the suggested regulation, which targeted only about 37 US banks with holdings of $100 billion in assets or more, would put young families’ dreams of home ownership and small businesses’ expansion plans at risk.”

Judging from the number of times the issue was raised at the Senate hearing, as well as the reaction of Powell, the campaign appears to be enjoying some success.

The issue appears to have produced a spilt between US financial regulatory authorities. The Basel III Endgame in the US is being overseen by the Fed, the Federal Insurance Deposit Insurance Corporation and the Office of the Comptroller of the Currency.

After significant changes have been made, due to objections raised by the banks, the position of Powell and the Fed is that more feedback should be solicited before it is put into effect. The other two agencies, as Powell has acknowledged, do not agree with that approach.

“My view, the strongly held view of the members of the board, is that we do need to put a revised proposal out for comment for some period,” he told the Senate Banking Committee.

Political considerations appear to be involved, according to a Reuters report on the issue. The other two agencies see the further review as “an unnecessary step that could delay the project with a presidential election just months away.”

Any lengthy delay could “imperil” the new rules, it continued, because a victory by Trump “could see him install some new regulators who are not supportive of the project.”

In any event, the new regulations are very much a case of shutting the farm door after the horse has bolted, because a new financial crisis will not be a repeat of 2008.

In the 16 years since that collapse, the global financial system has undergone massive changes with the rise of private equity firms. They are not only virtually unregulated but their operations and interconnections with the rest of the financial system are largely unknown and have been identified as a potential source of major turbulence.