

US central bank on course to tighten interest rates

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US President Trump spent years denouncing former Federal Reserve Board chair Jerome Powell as a “numbskull” and a “moron” for not lowering the central bank’s interest rate, possibly to as low as 1 percent.

But any hopes he might have had that Kevin Warsh, his appointee to the position, would immediately implement his change of course suffered a blow at the first meeting of the Federal Open Market Committee (FOMC) under his chairmanship.

In what was characterised as a “hawkish” decision, the FOMC yesterday removed the bias towards lowering rates in its statement on monetary policy with nine of its 19 members indicating, via their so-called “dot plots” where they pencil in projections, that they expect interest rates to rise by the end of the year. It decided to keep the present rate on hold.

This assessment, which did not include one from Warsh who is opposed to the practice, is a marked change from the start of the year when the forecast was for at least two rate cuts by the end of the year.

It was a significant shift from the last dot plot projections in March when no one forecast an interest rate rise this year.

The inflation set off by the war on Iran has changed the interest-rate settings by central banks around the world including the Fed. The Bank of Japan lifted its rate this week following a decision last week by the European Central Bank to up its rate by 0.25 percentage points, citing uncertainty created by the Iran war.

In its statement, the Fed did not specifically mention the war, saying only that inflation remained elevated above the goal of 2 percent, “in part reflecting supply shocks that have driven price increases in certain sectors, including energy,” and that the committee “will deliver price stability.”

Across the Atlantic, at a meeting of the G7 leaders in France, Trump more directly pointed to the forces at work when he outlined his reasons for deciding on an extension of the ceasefire deal with Iran, rather than continuing military action.

Trump told reporters that he had been influenced by the stock market and did not want to be compared to Herbert Hoover, the president at the time of the stock market crash of 1929 which ushered in the Great Depression.

“I didn’t want to see an economic catastrophe,” he said.

The reaction in the markets to the Fed decision was significant and swift. The S&P 500 closed 1.2 percent lower for the day and the NASDAQ was down 1.3 percent. The Dow fell by 1 percent to close 507 points lower.

There was a marked fall in consumer stocks—the *Wall Street Journal* described them as having “tumbled.”

This reflects the decline in real wages for the broad mass of the working population which means that consumption spending increasingly comes from the upper end of the income distribution. Figures released by the Bureau of Labor Statistics (BLS) earlier this month showed that a year and a half of wage increases for the average American worker had been wiped out by inflation caused by the rise in energy prices.

There was also a selloff in the bond market, with the yields (interest rates) on short-term Treasury debt rising to their highest levels in 16 months. The yield on the two-year Treasury bond jumped by 0.17 percentage points to 4.22 percent, its highest level since February 2025.

The yield on the 10-year bond, which is a key determinant for corporate borrowing costs and for

mortgages, also rose to above 4.5 percent.

Asked for his assessment of the Fed decision, which flew so directly in the face of his continued calls for cuts, Trump was relatively muted, saying he was prepared to be “guided” by Warsh on monetary policy.

And on the possibility of the Fed raising rates later in the year, he said: “It could happen. I mean it is hard to believe. It just keeps the country down. It is so unusual.”

The dot plot forecasts from members of the FOMC showed they expect an increase in inflation and slowing economic growth. The media forecast for inflation by the end of the year jumped to 3.6 percent from 2.7 percent. The expectation for core inflation, which excludes food and energy categories, rose to 3.3 percent from 2.7 percent.

The median outlook for growth in 2026 was lowered to 2.2 percent from the 2.4 percent forecast in March.

The decision by the Fed was unanimous—the first time there has been no dissent in a year. But there could well be differences below the surface, with Warsh referring to the two days of discussions as a “good family fight.”

Differences may well emerge on the plans being set in motion by Warsh to change the operations of the Fed.

He announced the setting up of a task force “in each of five areas central to the broad conduct of monetary policy.” These are: Fed communications; balance sheet policy; the use and reliance on existing data sources; productivity; and the Fed’s inflation framework.

Few details were given, as Warsh said he had yet to complete their establishment but gave some indication of the issues he wants to address.

One of the major changes he wants to see, in what he has called a “new chapter” for the Fed, is a reduction in its balance sheet to levels more akin to those that prevailed before the financial crisis of 2008.

This has been a long-standing aim, but it has already been opposed by other members of the Fed’s governing body. Fed governor Christopher Waller has described the return to this position as “inefficient” and “stupid.”

He also indicated that press conferences after every Fed meeting may also be scrapped because “you want to make sure you have something important to say.”

And he wants to move away from agencies such as the BLS because the current sources only provided “echoes of history” rather than real-time information

used by corporations on which to base decisions.

This was coupled with a significant statement, one which would never have been made by Powell or any of his predecessors, who always sought to create the image that Fed operations were based on developments in the real economy and the interests of the American people, and that while it took note of the markets, it was not directed by them.

Setting out his new orientation, Warsh said: “Financial market prices are probably the most important source of information to guide central bankers.”



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