Fed raises interest rates, showing confidence in health of economy

By Binyamin Appelbaum
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The Federal Reserve raised its benchmark interest rate on Wednesday and signaled that it expects additional rate increases next year in a display of measured confidence in the economy that came despite financial market worries and political pressure to suspend rate increases.

Jerome H. Powell, the Fed's chairman, emphasized the continued strength of economic growth at a news conference after the announcement. He acknowledged new strains in recent months, including weaker growth in Europe and China and a downturn in stock prices, and he said the Fed expects slightly slower domestic growth and fewer rate increases next year.

But he strongly defended the Fed's decision to increase rates.

"We think this move was appropriate for what is a very healthy economy," Mr. Powell said.

Mr. Powell's remarks were described by one analyst as a dose of "tough love" for financial markets.

Mr. Powell insisted on the wisdom of the Fed's plans to raise borrowing costs while investors dumped their holdings. Stock prices fell when the Fed released its policy statement at 2 p.m., and dropped again as Mr. Powell spoke. The S&P 500 was down 1.5 percent on the day and is now down 6 percent on the year.

The Fed's decision also rebuffed President Trump, who has broken with the practice of his predecessors by loudly and publicly campaigning for the Fed to keep rates low to continue stimulating the economy. "Feel the market, don't just go by meaningless numbers," Mr. Trump urged in a tweet earlier on Tuesday.

Asked about Mr. Trump's advice, Mr. Powell said it "played no role" in the Fed's decision.

"Nothing will deter us from doing exactly what we think is the right thing to do," he said.

The decision to raise rates for the fifth consecutive quarter, by a unanimous vote of the Federal Open Market Committee, amounted to a rejection of the view that the Fed should continue to stimulate the economy in the hope of increasing employment and wage gains. The benchmark rate will now sit in a range from 2.25 percent to 2.5 percent, abutting the lower end of what Fed officials consider the neutral zone: the region in which rates would neither stimulate nor restrain the economy.

"Policy at this point does not need to be accommodative," Mr. Powell said of that milestone.

The Fed's announcement offered a few crumbs for critics. In previous statements, the Fed had said it planned "further gradual increases" in its benchmark rate, conveying to investors that additional increases were expected. Wednesday's statement sought to recalibrate those expectations by adding the word "some" to the beginning of the phrase, suggesting that rates may not rise much higher.

A majority of Fed officials predicted on Wednesday that the central bank would raise rates no more than twice next year. In September, most Fed officials had predicted at least three rate increases.

Mr. Powell tried to emphasize that the Fed would continue to keep a close eye on economic conditions and said that the ultimate pace of rate increases was "not predetermined." He has said the Fed's goal is to strike a balance

between extending the expansion and maintaining control of inflation.

But the overall tone of the statement suggested the Fed continues to regard the strength of economic growth as more impressive than any storm clouds on the horizon, including a trade war with China and geopolitical strains overseas. Companies continue to add jobs, the unemployment rate sits at 3.7 percent and wages are rising more quickly.

"Over the past year, the economy has been growing at a strong pace, the unemployment rate has been near record lows and inflation has been low and stable," Mr. Powell said. "All of those things remain true today."

Still, Mr. Powell noted that the robust expansion of 2018 would most likely moderate next year, and critics continued to raise questions about the Fed's steady march toward higher rates. It now appears likely that inflation will fall short of the Fed's 2 percent annual target for the seventh consecutive year. And Fed officials predicted on Wednesday that the central bank will miss the 2 percent target next year, too.

Low inflation is a sign of economic weakness and can be a problem in its own right, for instance by restricting the Fed's ability to reduce borrowing costs should the economy begin to falter.

"I think they will look back on this as a mistake," Josh Bivens, the director of research at the left-leaning Economic Policy Institute, said of the rate increase. "This threatens to snuff out the very beginning of wage gains that we've started to see recently in the data. The Fed should allow the expansion's gains to reach more broadly into the work force and get off the steady escalator of ever-higher interest rates."

Investors and some economists are increasingly concerned about the economic outlook, particularly as the sugar high from Mr. Trump's $1.5 trillion tax cut and spending increases wears off and as the president continues to press trade fights with most of the nation's major trading partners.

On Wednesday, a group of United States financial regulators — which includes the Fed — warned that the trade fight with China had the potential to "materially impact U.S. economic growth."

FedEx, a bellwether for the global economy, on Wednesday sharply reduced its profit outlook for 2019 and announced plans to cut jobs, citing a deterioration in demand for its shipping services.

Fred Smith, the company's chief executive, blamed the Trump administration's trade policies.

"Most of the issues that we're dealing with today are induced by bad political choices," Mr. Smith said, specifically citing Mr. Trump's decisions to impose tariffs on a wide range of foreign goods.

There are also signs that the Fed's march toward higher rates is weighing on sales of homes and autos.

"The era of low auto loan rates is clearly behind us," said Jonathan Smoke, chief economist at Cox Automotive, which gathers data on the auto industry. Mr. Smoke said the average monthly payment on a new car in November was $567, a 5 percent increase over November 2017. "If rates are indeed even higher in 2019, the buyer pool for new vehicles could further decline," he said.

Mortgage rates, less directly tied to Fed policy, have also climbed, contributing to a recent softening in the sales of new and existing homes. The average interest rate on a 30-year fixed-rate mortgage was 4.63 percent last week, up from 3.93 percent a year ago, according to Freddie Mac.

Mr. Powell said these developments "may signal some softening relative to what we were expecting a few months ago." He added that he was aware of the increasingly dour mood

among business executives. A survey of corporate chief financial officers published by Duke University last week found that almost half expected the economy to enter a recession next year.

“There’s a mood of concern, a mood of angst about growth going forward,” Mr. Powell said.

But he said the impact on the economy so far appeared to be small.

“In our view, these developments have not fundamentally altered the outlook,” Mr. Powell said.

He added that the United States economy “has continued to perform well” and that — while overall financial conditions have tightened — the Fed has only “modestly” lowered its projections as a result.

The bottom line, he said, is that the Fed intends to let circumstances dictate its decisions.

If the economy weakens, the Fed will raise rates more slowly, or stand still. If the economy continues to chug along, the Fed is likely to raise rates at least a few more times.

The Fed’s forecasts are guesses, not promises. “There’s a fairly high degree of uncertainty about both the path and the ultimate destination of any further increases,” Mr. Powell said.