THE WALL STREET JOURNAL.

ECONOMY | U.S. ECONOMY

Fed Signals Low Rates Likely to Last Several Years

Central bank also sets high hurdles for raising rates going forward

'These changes clarify our strong commitment over a longer time horizon,' said Fed Chairman Jerome Powell at a virtual news conference Wednesday.
PHOTO: DANIEL ACKER/BLOOMBERG NEWS

By Nick Timiraos
Updated Sept. 16, 2020 8:30 pm ET

SAVE PRINT TEXT 209

WASHINGTON—The Federal Reserve pledged to support the economic recovery by setting a higher bar to raise interest rates and by signaling it expected to hold rates near zero for at least three more years.

In new projections released Wednesday after a two-day policy meeting, all 17 officials who participated said they expect to keep rates near zero at least through next year, and 13 projected rates would stay there through 2023.

The Fed's rate-setting committee also revised its postmeeting statement to specify it would maintain rates near zero until it sees evidence of a tight labor market and inflation reaches 2% "and is on track to moderately exceed 2% for some time."

"They set an enormously high bar to raise rates here. That's the bottom line," said Roberto Perli, a former Fed economist who is now at research firm Cornerstone Macro.

U.S. stock gains slipped away Wednesday afternoon. The S&P 500 fell 0.5% as of the 4 p.m. close of trading in New York. The yield on the benchmark 10-year U.S. Treasury was little changed, ticking up to 0.686%, from 0.678%. After topsy-turvy trading in recent days, the major U.S. stock indexes are all down so far this month.

The Fed's two-day policy meeting that concluded Wednesday is the first since officials last month announced a new policy framework that abandoned their longtime strategy of pre-emptively lifting interest rates to head off higher inflation.

The latest materials from the Fed revealed just how much the central bank expects to change the way it will react to improvements in the economy.

The new economic projections, for example, showed most officials expected interest rates to stay near zero over the next three years, even if inflation reaches 2% and the unemployment falls to around 4%.

By contrast, when the Fed lifted interest rates at the end of 2015 after holding them near zero for seven years, officials projected unemployment would end the year around 5% and so-called core inflation, which excludes volatile food and energy prices, would end the year at 1.3% and wouldn't reach 2% for three more years.

"These changes clarify our strong commitment over a longer time horizon," said Fed Chairman Jerome Powell at a news conference. "I'm not looking for a big reaction right now. But I think over time, guidance that we expect to retain the current stance until the economy has moved very far toward our goals is a strong and powerful thing."

RELATED

- Heard on the Street: Is the Fed Just Seeing Shadows—Or Should We Be Worried?
- Stocks Rise After Fed's Decision
- Mortgage Securities Flood the Market
- Why Fed Officials Are Pushing for More Stimulus From Lawmakers (Sept. 13)
- Fed Approves Shift on Inflation Goal, Ushering In Longer Era of Low Rates(Aug. 27)
- Fed Cuts Rates to Near Zero and Will Relaunch Bond-Buying Program (March 15)

Separately, officials revised their June economic forecasts to reflect expectations of a less severe contraction this year and a lower unemployment rate. They now project unemployment will average around 7% to 8% during the last three months of this year, down from June projections of around 9% to 10%.

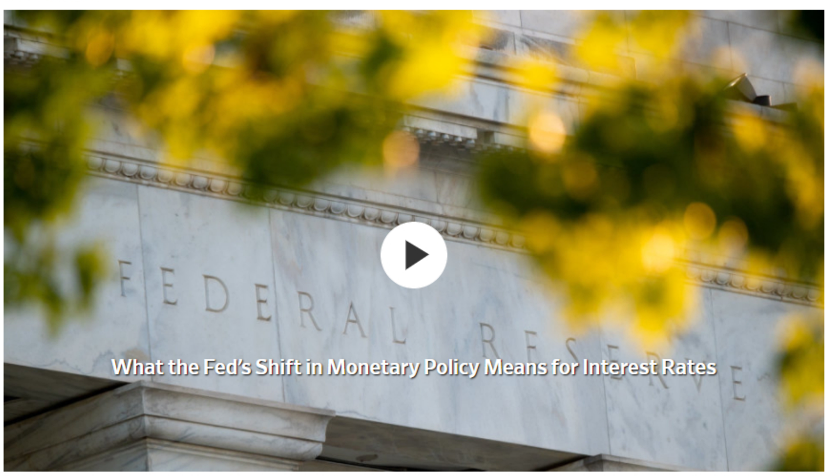
The unemployment rate fell to 8.4% last month from a recent high of 14.7% in April. Mr. Powell said it was possible that the lower level of the rate partly reflects fewer Americans looking for work right now, which means they aren't formally counted among the jobless.

Fed officials indicated concern that easy gains from reopening the economy could mask deeper scars, as the most vulnerable businesses shut down and employees in hard-hit sectors face longer spells of joblessness.

The ranks of temporarily laid-off workers have fallen by two-thirds, or around 12 million, since the spring. But more than two million Americans have permanently lost their jobs and 11 million fewer Americans were employed last month than in February.

Mr. Powell said it would be important for Congress to spend more money to support these households, along with hard-hit businesses and state and local governments, to limit additional damage to the economy.

Related Video



Federal Reserve Chairman Jerome Powell announced in late August a major shift in how the central bank sets interest rates. WSJ's Greg Ip explains the strategy behind the changes and what they mean for consumers. Photo: Erin Scott/Bloomberg

"For the last 60 days or so, the economy's recovered faster than expected, and that may

Federal Reserve Chairman Jerome Powell announced in late August a major shift in how the central bank sets interest rates. WSJ's Greg Ip explains the strategy behind the changes and what they mean for consumers. Photo: Erin Scott/Bloomberg

"For the last 60 days or so, the economy's recovered faster than expected, and that may continue or not. We just don't know," said Mr. Powell.

The Fed cut rates to near zero in March and has purchased trillions of dollars of securities after the coronavirus pandemic threatened to touch off a financial panic after investors and businesses sought to raise cash. It also backstopped an array of lending markets.

But with short- and long-term interest rates at historically low levels, the Fed could have fewer tools to spur a recovery than it did after the 2008 financial crisis. At Wednesday's news conference, Mr. Powell used the word "powerful" 10 times to describe the Fed's new guidance.

A big question heading into this week's meeting was whether the Fed would detail the specific conditions that might prompt an end to near-zero interest rates. Such so-called forward guidance is one way officials believe they can provide more stimulus.

Several Fed reserve bank presidents had said they were in no rush to do this because they wanted to have more clarity about the economic outlook and because investors already expect the Fed to keep rates low for several years.

But others said this guidance needed to build on their new policy framework by spelling out the inflation and labor-market conditions consistent with keeping rates near zero. These steps could help convince markets that the Fed won't raise rates aggressively even after the coronavirus has been controlled and the economy is on sturdier footing.

"The Federal Reserve is digging a firebreak to ensure that market participants do not get ahead of themselves and come to expect [higher interest rates] sooner than policy makers think appropriate," said Vincent Reinhart, a former Fed economist who is now chief economist at Mellon. "And what they think is that it will be a long time before they let off the gas."

Two of 10 voting officials dissented from the statement . Dallas Fed President Robert Kaplan didn't want to make the guidance more specific right now, while Minneapolis Fed President Neel Kashkari preferred a simpler formulation.

The dissents "unveil the reality that the committee is not on the same page, which could presage some problems down the road," said Mr. Perli. But they also showed Mr. Powell and the leadership of the committee "felt that this was the right thing to do."

Mr. Powell said differences weren't unusual given the novelty of the Fed's new framework. "We're the first major central bank to adopt this framework. There's no cookbook," he said. "So of course, there would be a wide range of views."

SHARE YOUR THOUGHTS

What do you find most notable about the Fed's economic projections? Join the conversation below.

Under its new framework, the Fed says that following periods when inflation has run persistently below its 2% target, officials will want inflation to run "moderately" above 2% for "some time." The Fed's policy statement adopted similar language Wednesday.

Mr. Powell, when pressed, declined to define those modifiers.

"Where it starts to get tricky is the market is going to want a bit more of what it means to moderately overshoot 2% and what it means to do so for some time," said Michelle Meyer, an economist at Bank of America.

Fed officials hope their policy will help by influencing expectations of future inflation by investors, consumers and businesses. They want to avoid the conditions that have hampered Europe for part of the last decade and Japan for most of the last two decades as lower inflation leads to lower interest rates.

"This isn't some idle academic theory. This is what's happening all over the world," said Mr. Powell.

Write to Nick Timiraos at nick.timiraos@wsj.com

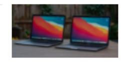
Appeared in the September 17, 2020, print edition as 'Fed Sets Higher Hurdles For Rate Increase.'

Stocks Slip After Dow, S&P Hit Record

Republicans Re-Elect Kevin McCarthy as House Minority Leader

Walmart's Sales Gains Slow as Pandemic Drags On

Apple's M1 MacBook Air and MacBook Pro Review: The Laptop's Biggest Leap in Years



Biden's Path Forward at DHS Faces Competing Pressures

Market Moves

HEALTH

Moderna and Pfizer Are Reinventing Vaccines, Starting With Covid

CREDIT MARKETS

Falling 'Real' Yields Drive Investors to Junk Bonds