The Daily Dish

Trump, the Fed, and Growth

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Eakinomics: Trump, the Fed, and Growth

President Trump is at it again, criticizing the Federal Reserve's pace of normalization and telling *The Wall Street Journal*, "'Every time we do something great, (Fed Chairman Powell) raises the interest rates,' …adding that Mr. Powell 'almost looks like he's happy raising interest rates.'" The Fed has raised rates seven times since the president took office — three under Chairman Powell — and is expected to do so again in December. But with the federal funds target range between 2.0 and 2.25 percent and inflation at about 2.0 percent, the real federal funds rate is essentially zero. It is hard to argue that this constitutes excessive tightness. (One could adjust this a bit north because the Fed is simultaneously selling off its large portfolio of Treasuries and mortgage-backed securities, but this adds only 25 additional basis points.)

So the argument seems wrong on the merits. But the president is entitled to his opinion and many presidents have tried to lobby the Fed on its policy moves. Historically, however, this took place in private Oval Office meetings or, more frequently, quietly via subordinates like the Treasury Secretary or Chairman of the Council of Economic Advisers. The president's public questioning of the Fed's moves is quite different. It is an open challenge to its competence, at a minimum. Even more, his assertion that it hikes rates "every time we do something great" attributes an anti-administration motive to the Fed. This is damaging because it is diametrically opposed to the confidence that the U.S. public needs in its monetary authority — especially when it is delivering bad news.

That moment will come, if not in 2018 or 2019 then at some point between now and 2024 — the end of the second term the president aspires to. When the Fed does proactively tighten, it will do so to enhance the growth prospects by controlling inflation expectations and financial conditions. President Trump will be one of the beneficiaries of such a move. It is short-sighted for him to undercut the Fed's ability to execute policies from which he will benefit.

If the president wants continued strong growth, he should abandon his failed trade strategy. As the chart below shows, a very troubling aspect of the most recent data on gross domestic product was the decline in the pace of growth of non-residential fixed investment — i.e., business investment. This is new weakness in a series that had strengthened every quarter of the Trump Administration. That growth was fueled by regulatory restraint, the Tax Cuts and Jobs Act, and a market-oriented energy policy. But more recently, the steady drip, drip, drip of tariffs, retaliation, and trade-war talk has damaged the business community's willingness to undertake rapid expansion. The decline is even more troubling in light of the weak condition of the residential sector (see below) — a traditional source of cyclical strength.

The key to pro-growth policy is restraint. At every point when the president has to choose between other policy objectives and growth, he needs to pick growth. This was the failing of the Obama Administration, which readily chose social issues (the Affordable Care Act), a labor agenda (joint employer, etc.), and environmental issues (the Clean Power Plan) over growth. The result was poor growth. At present, the president needs to choose growth over voicing his opinion.