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Yellen Sets a Familiar Direction for the Fed

By Binyamin Appelbaum
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WASHINGTON — Janet L. Yellen, the new chairwoman of the Federal Reserve, told a House committee on Tuesday that she strongly supported and planned to continue the policies adopted under her predecessor, Ben S. Bernanke.

At the same time, in emphasizing her concern about unemployment — and in agreeing to spend almost six hours answering the committee's questions — Ms. Yellen also began the delicate process of imposing her own influence on the Fed's direction.

Ms. Yellen made clear that the Fed planned to keep cutting back on its bond buying, which had been a crucial part of its economic stimulus campaign, unless there was a "notable change" in the economy toward a more negative outlook. "I served on the committee as we formulated our current policy strategy, and I strongly support that strategy," she said.

But she described the recovery of the labor market as "far from complete," and said she retained her longstanding conviction that the Fed had the power to improve the situation. That suggests the Fed may continue to strengthen the mainstay of its campaign, keeping short-term interest rates at extraordinarily low levels.

Ms. Yellen's marathon testimony was a statement in the same vein. As the Fed's vice chairwoman, she pushed to increase communication with investors and the public, reflecting her view that clear communication enhances the power of monetary policy. Communication, in the form of assurances that the Fed intends to keep rates low, is now the Fed's primary means of suppressing rates.

The stock markets rose in the morning following the release of Ms. Yellen's testimony, and again when she began to speak. Some analysts speculated that investors were reassured by the message of continuity. The news that House Republicans planned to allow a debt ceiling increase reinforced the good mood on Wall Street. The Standard & Poor's 500-stock index rose 19.91 points, or 1.1 percent, to close at 1,819.75.

Similarly, the Dow Jones industrial average rose 192.98 points, or 1.2 percent, to close at 15,994.77. The Nasdaq composite increased 42.87 points, or 1 percent, to 4,191.05.

In the bond market, the yield on the Treasury's 10-year note rose to 2.73 percent, from 2.67 percent late Monday. Its price fell 16/32, to 100 6/32.

Ms. Yellen, in her inaugural public appearance as Fed chairwoman, was fluid in discussing monetary policy, but appeared less assured in answering questions about financial regulation. She sometimes consulted a binder that she kept open on the witness table and at times turned to ask questions of her aides.

"The work of making the financial system more robust has not yet been completed," she said, but she mostly skirted questions about the details.

She faced some confrontational questions, particularly from Republicans concerned the Fed's stimulus campaign was doing more harm than good, by seeding inflation, starving savers of income and destabilizing financial markets.

Rep. Tom Cotton, an Arkansas Republican, played a video message from a 76-year-old veteran inviting Ms. Yellen to a town-hall meeting to discuss low interest rates.

By contrast, some Democrats questioned whether the Fed could do more to cut unemployment. "I hope you will press your colleagues on the Federal Open Market Committee to take into account the ongoing impact that this long-term unemployment crisis is having on millions of American families," said Rep. Maxine Waters of California, the ranking Democrat on the House committee.

But Ms. Yellen appeared to disarm the committee members by agreeing to stay as long as they liked. It took almost six hours to field questions from every interested member of the Financial Services Committee — one of the largest House committees, in part because lawmakers clamor to be on it because they can raise money from the financial services industry.

Members thanked her for her time and several mentioned that their daughters said her very presence was an inspiration.

The harshest criticism came after Ms. Yellen left, when a panel of experts was called to comment on the Fed's performance.

The central bank's stimulus campaign has "driven up asset prices without adding significantly to job creation," said Mark Calabria, director of financial regulation at the Cato Institute. He said low borrowing costs might be making it easier for companies to invest in technology rather than hiring workers.

The economy remains scarred by the collapse of the housing bubble and the consequent 2008 financial crisis. Growth is tepid, unemployment high, inflation sluggish. Ms. Yellen acknowledged those problems, but reiterated the Fed's upbeat forecast.

“The economic recovery gained greater traction in the second half of last year,” she said, citing the growth of spending by consumers and businesses. She said the Fed expected “economic activity and unemployment will expand at a moderate pace this year and next.”

Ms. Yellen acknowledged that she was “surprised” by disappointing estimates of job growth in December and January, but she cautioned against “jumping to conclusions” in assessing the longer-term trend. She noted the government would release an estimate of February job growth before the Fed’s March meeting.

She played down concerns about the consequences of Fed policy. Asked about the impact of low interest rates on savers, particularly the elderly, she said that the Fed could not raise rates without damaging the economy, and noted that low rates had a variety of effects. Retirees with savings accounts, for example, often own stocks too, which have soared in recent years.

Like her predecessor, Ms. Yellen said the Fed’s greatest concern was the risk of destabilizing financial markets. And like Mr. Bernanke, she said the Fed was watching closely but didn’t see problems yet. “I haven’t seen threats to financial stability that have built to the point of flashing orange or red,” Ms. Yellen said.

The Fed said in 2012 that it planned to keep short-term interest rates near zero at least as long as the unemployment rate remained above 6.5 percent. It has since said that it was likely to maintain that policy well past that threshold, but with the unemployment rate reaching 6.6 percent in January, some Fed officials have said there is a need for greater clarity about its plans.

To provide that clarity, however, the Fed must first resolve an internal debate. Much of the decline in the unemployment rate was because people have stopped looking for work. The share of Americans with jobs has not increased since the recession.

Changing demographics, including the aging of the baby boom, is part of the explanation. Some Fed officials see it as the prime cause. “While I do expect some discouraged workers to re-enter the labor force as the economy improves, I still believe the overall unemployment rate remains a good summary statistic of labor market conditions,” Charles Plosser, president of the Federal Reserve Bank of Philadelphia, said in a speech Tuesday in Newark, Del.

“Continuing to buy assets is neither helpful nor essential,” Mr Plosser said.

Other officials, however, predict that a significant number of Americans will return to the labor market as the economy improves, helping keep a lid on inflation.

Ms. Yellen, asked about the issue, appeared to place a greater emphasis on economic factors. She said demographics explained “a significant part of the decline.”

But she continued, with typical caution, “There may also be, and I am inclined to believe myself based on the evidence, that there are also cyclical factors at work.”