United States Senate
WASHINGTON, DC 20510

June 10, 2024

The Honorable Jerome Powell
Chair
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Dear Chair Powell:

We write today to urge the Federal Reserve (the Fed) to cut the federal funds rate from its current, two-decade-high of 5.5 percent.[1] This sustained period of high interest rates is already slowing the economy and is failing to address the remaining key drivers of inflation. Furthermore, the European Central Bank (ECB), which like the Fed has a mandate to steer inflation towards a target of 2%, cut interest rates for the first time in five years.[2] It's time for the Fed to do the same.

Major central banks have cut rates or are leaning towards lowering interest rates.[3] The ECB cut its interest rates on Thursday from 4% to 3.75%.[4] On Wednesday, the Bank of Canada, cut rates becoming the first of the Group of Seven (G7) nations to do so.[5] Sweden, Switzerland, Hungary and the Czech Republic have already cut rates.[6] The Fed's decision to keep interest rates highs continues to widen the rate gap between Europe and the U.S, as the lower interest rates could push the dollar higher, tightening financial conditions.[7]

The Fed's current interest rate policy is also having the opposite of its intended effect: it is driving up housing and auto insurance costs, which are currently the main drivers of the overall inflation rate.[8] Indeed, "[e]xcluding shelter, overall PCE[, the Fed's preferred inflation measure,] would have increased by 1.8 percent in April, below the Fed's target… What's more, PCE

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[1] Federal Reserve System, "Federal Reserve Issues FOMC statement," March 20, 2024, https://www.federalreserve.gov/newsevents/pressreleases/monetary20240320a.htm.
[2] European Central Bank, "Monetary policy," https://www.ecb.europa.eu/ecb/orga/tasks/monpol/html/index.en.html#:~:text=We%20keep%20prices%20stable%20by,2%25%20over%20the%20medium%20term; Wall Street Journal, "ECB Cuts Interest Rates for First Time Since 2019," Tom Fairless and Paul Kiernan, June 6, 2024, https://www.wsj.com/economy/central-banking/ecb-cuts-interest-rates-for-first-time-since-2019-b2707c65.
[3] *Id.*
[4] *Id.*
[5] Reuters, "Canada becomes first G7 nation to cut interest rates," Promit Mukherjee and David Ljunggren, June 5, 20224, https://www.reuters.com/markets/rates-bonds/bank-canada-cuts-rates-first-time-four-years-2024-06-05/.
[6] Wall Street Journal, "ECB Cuts Interest Rates for First Time Since 2019," Tom Fairless and Paul Kiernan, June 6, 2024, https://www.wsj.com/economy/central-banking/ecb-cuts-interest-rates-for-first-time-since-2019-b2707c65; AP News, "Europe Central Bank jumps ahead of the Fed in lowering rates. But future cuts may be limited," David Mchugh, June 6, 2024, https://apnews.com/article/european-central-bank-interest-rates-cut-087f5a0eb5caf841266afb16c65e520b.
[7] New York Times, "E.C.B. Is likely to Leapfrog the Fed on Interest Rate Cuts," Eshe Nelson, June 5, 2024, https://www.nytimes.com/2024/06/05/business/european-central-bank-interest-rates.html.

excluding shelter has been running at 2 percent or less since October."[9] This housing-related inflation is directly driven by high interest rates: reducing rates will reduce the costs of renting, buying, and building housing, lowering Americans' single highest monthly expense. Lowering interest rates will likely also decrease the cost of auto insurance as well, which has risen due to factors completely unrelated to the cost of lending.[10]

In addition to having the opposite of its intended effect, the Fed's decision to keep interest rates high continues to threaten the economy.[11] Many economists agree that "inflation has fallen enough that the Fed should start cutting rates before it causes more severe economic damage."[12] Mark Zandi, Chief Economist of Moody's Analytics, highlighted "those [high interest] rates are like a corrosive on the economy; you know, they wear the economy down, and at some point, something could break."[13] Additionally, Zandi has urged you not to "sacrifice the economy on the altar of the 2% target"[14] and noted that while layoffs are currently low, "that's next on businesses' to do list."[15] J.P. Morgan analysts have argued that the Fed's current rates may even be fueling inflation and that prices will only stabilize once the central bank starts cutting rates.[16] Participants in the FOMC's May meeting also noted that "the high interest rates could contribute to vulnerabilities in the financial system."[17]

Shelter inflation accounts for a significant portion of the Consumer Price Index (CPI), and high interest rates are resulting in higher, not lower, shelter costs.[18] High interest rates have driven up rental prices, mortgages, and construction costs, limiting the supply of housing and keeping

[8] Bancreek Capital Advisors, "Checking the tape – key takeaways from April 2024 PCE inflation," May 31, 2024, https://www.bancreek.com/p/april-2024-pce-update.

[9] Boston Globe, "Rising housing costs are the problem. So that means it's time for the Fed to lower interest rates," Larry Edelman, June 3, 2024, https://www.bostonglobe.com/2024/06/03/business/federal-reserve-inflation-housing-costs/.

[10] The American Prospect, "Inflation, Misguided Economics, and the Fed," Robert Kuttner, May 15, 2024, https://prospect.org/blogs-and-newsletters/tap/2024-05-15-inflation-misguided-economics-fed/.

[11] Federal Reserve Board, "Transcript of Chair Powell's Press Conference May 1, 2024," p. 3, https://www.federalreserve.gov/mediacenter/files/FOMCpresconf20240501.pdf.

[12] New York Times, "High Interest Rates Are Hitting Poorer Americans the Hardest," Ben Casselman and Jeanna Smialek, May 14, 2024, https://www.nytimes.com/2024/05/14/business/economy/interest-rates-inequality.html; Bloomberg, "Goldman Axes Bet on July Fed Cut as Market Sees Less Easing," May 24, 2024, https://www.bloomberg.com/news/articles/2024-05-24/goldman-pushes-first-fed-rate-cut-call-to-september-from-july-lwkl2exr; InvestmentNews, "Morgan Stanley economist says Fed will cut in June," April 4, 2024, https://www.investmentnews.com/investing/news/morgan-stanley-economist-says-fed-will-cut-in-june-251838.

[13] Business Insider, "'Something could break': The Fed risks recession, bank failures if it doesn't cut rates soon, economist Mark Zandi says," Jennifer Sor, May 10, 2024, https://www.businessinsider.com/fed-recession-bank-failures-economy-rate-cuts-outlook-loans-moodys-2024-5#:~:text=%22Those%20rates%20are%20corrosive%20on,%2C%22%20the%20top%20economist%20said.

[14] USA Today, "Should the Fed relax its 2% inflation goal and cut interest rates? Yes, some experts say," Paul Davidson, https://www.usatoday.com/story/money/2024/05/20/fed-inflation-goal-too-rigid/73718450007/.

[15] Tweet by Mark Zandi, May 5, 2024, https://x.com/Markzandi/status/1787099516551725159.

[16] Unusual Whales, "JPMorgan, $JPM, has made the case that high rates are actually driving inflation," April 26, 2024, https://unusualwhales.com/news/jpmorgan-jpm-has-made-the-case-that-high-rates-are-actually-driving-inflation-per-bloomberg.

[17] Federal Reserve Board, "Minutes of the Federal Open Market Committee April 30-May 1, 2024," May 1, 2024, p. 8, https://www.federalreserve.gov/monetarypolicy/files/fomcminutes20240501.pdf.

[18] The American Prospect, "Inflation, Misguided Economics, and the Fed," Robert Kuttner, May 15, 2024, https://prospect.org/blogs-and-newsletters/tap/2024-05-15-inflation-misguided-economics-fed/.

prices high.[19] Zandi emphasized that if "rent for single-family homes is removed from the Fed's preferred price measure, inflation is already below 2%."[20]

The core problem is that "[t]he Fed's interest rate tool is not very well matched for housing inflation and, if anything, [] [exacerbates] the housing inflation."[21] The inventory of single-family homes has decreased by 75% from its peak of 4 million to approximately 1 million today.[22] Higher interest rates are particularly hurting young adults (ages 18-35) who are trying to become homeowners, reflected in the nearly 10% decrease in homeownership among this age bracket compared to the young people of previous generations.[23] Lower mortgage rates would encourage more people to sell their homes, which would in turn increase housing supply, decrease prices, ease the costs of renting, and ultimately increase homeownership.[24]

High interest rates are also further increasing construction costs, which are causing developers to cancel, significantly delay, or put on hold an increasing number of projects across the country,[25] "aggravat[ing] [the housing] shortage by raising credit costs to builders and developers."[26] The country is already facing a severe housing shortage, and the Fed's refusal to bring down interest rates is exacerbating this shortage and driving higher inflation rates.[27]

The Fed's interest rate increase also appears to be the wrong tool to reduce other factors driving inflation, such as auto insurance. Overall inflation would have been "only half a percentage point away" from the Fed's desired 2 percent if auto insurance was excluded.[28] But the increase in the cost of motor vehicle insurance reflects factors including a shortage of mechanics, more severe and frequent car accidents, climate change leading to more vehicles damaged by extreme

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[19] Letter from Senator Warren, Hickenlooper, Rosen, and Whitehouse to Chair Powell, January 28, 2024, https://www.warren.senate.gov/imo/media/doc/2024.01.28%20Letter%20to%20Federal%20Reserve%20on%20Housing%20Market.pdf.

[20] USA Today, "Should the Fed relax its 2% inflation goal and cut interest rates? Yes, some experts say," Paul Davidson, https://www.usatoday.com/story/money/2024/05/20/fed-inflation-goal-too-rigid/73718450007/.

[21] Tweet by Groundwork Collaborative, April 11, 2024, https://twitter.com/Groundwork/status/1778506284695748751.

[22] The BIG Picture, "Why the FED Should Be Already Cutting," Barry Ritholtz, May 2, 2024, https://ritholtz.com/2024/05/fed-cutting-oer/; HousingWire, "Have we already reached peak home sales for the year?," Logan Mohtashami, March 21, 2024, https://www.housingwire.com/articles/have-we-already-reached-peak-home-sales-for-the-year/.

[23] Urban Institute, "Five Ways Congress Can Support Young Homebuyers," Jung Hyun Choi and Aniket Mehrotra, May 2024, https://www.urban.org/sites/default/files/2024-05/Five_Ways_Congress_Can_Support_Young_Homebuyers.pdf.

[24] *Id.*

[25] USA Today, "High interest rates take growing toll as planned apartments, wind farms, shops are scrapped," Paul Davidson, May 15, 2024, https://www.usatoday.com/story/money/2024/05/15/high-interest-rates-inflation-cancel-construction/73637163007/.

[26] The American Prospect, "Inflation, Misguided Economics, and the Fed," Robert Kuttner, May 15, 2024, https://prospect.org/blogs-and-newsletters/tap/2024-05-15-inflation-misguided-economics-fed/.

[27] Forbes, "Interest Rates In 2024: Which Sectors Will Benefit If Rates Stay High," Jason Kirsch, https://www.forbes.com/sites/investor-hub/article/interest-rates-2024-which-sectors-will-benefit-rates-high/?sh=21aa6563294e.

[28] New York Times, "Auto Insurance Spike Hampers the Inflation Fight," Talmon Joseph Smith, February 29, 2024, https://www.nytimes.com/2024/02/29/business/economy/auto-insurance-inflation.html.

weather, and more complex cars that are more expensive to repair.[29] None of these factors are mitigated by high interest rates. In fact, the Fed's rapid increase in interest rates in 2022 may have had the opposite of its desired effect, prompting insurers to raise premiums.[30] According to one analysis:

> This could also be another area where Federal Reserve interest increases may have worsened the problem. Insurance companies invest premiums as "float" before they have to pay anything back out in claims. When interest rates began to jump, insurance companies were caught short with investments in long-term securities that ended up losing money. In other words, industry losses have in one sense nothing to do with higher costs for auto repairs, but rather with their own bad investment strategies.[31]

The Fed's monetary policy is not helping to reduce inflation. Indeed, it is driving up housing and auto insurance costs—two of the key drivers of inflation—threatening the health of the economy and risking a recession that could push thousands of American workers out of their jobs. You have kept interest rates too high for too long: it is time to cut rates.

Thank you for your attention to this matter.

Sincerely,

Elizabeth Warren
United States Senator

Jacky Rosen
United States Senator

[29] CBS News, "Car insurance premiums around the U.S. are soaring. Here's why.," Kate Gibson, January 12, 2024, https://www.cbsnews.com/news/car-insurance-rates-inflation-costs/; CNN Business, "What's behind the rapid increase in car insurance rates," Elizabeth Buchwald, March 13, 2024, https://www.cnn.com/2024/03/13/business/car-insurance-rates-are-surging/index.html.

[30] New York Times, "Auto Insurance Spike Hampers the Inflation Fight," Talmon Joseph Smith, February 29, 2024, https://www.nytimes.com/2024/02/29/business/economy/auto-insurance-inflation.html.

[31] The American Prospect, "Why Auto Insurance Rates Are Out of Control," David Dayen, May 16, 2024, https://prospect.org/economy/2024-05-16-auto-insurance-rates-out-of-control/.

John Hickenlooper
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