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Jerome Powell gambles he won't have to raise rates in Trump's term.

The Fed Thinks Inflation Is Vanquished

Federal Reserve Chairman Jerome Powell is sticking with his view that inflation is all but vanquished. The interest--rate cut he delivered Thursday marks a gamble that he won't need to raise rates early in the next Trump Administration.

The 25-basis-point cut in the fed funds rate target range, to 4.5%-4.75%, is a head-scratcher on the economic merits. Mr. Powell delivered a surprisingly large, 50-basis point cut in September despite persistent above-target inflation and a strong labor market. Long bond rates promptly popped and for the most part have kept rising. That wasn't the goal. *

Mr. Powell struggled Thursday to explain why a further cut is warranted when inflation remains well above the 2% target. It's been 2.7% year-on-year for four of the past five months, according to the Fed's preferred personal-consumption- expenditure index. *

The Fed is saying, "trust our spreadsheets." Economic models tell Mr. Powell and colleagues that inflation will resume its downward drift eventually, and that if they don't cut rates in the meantime the labor market will soften more than they intend. *

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That's a lot of faith to put in economic models that missed most developments in this inflationary cycle, including the initial arrival of the inflation in 2021 and a false rate-cut dawn last winter. Contrary to what the Fed says, there's not much evidence that financial conditions are tight. Equities, commodities, real-estate prices and plenty of other data point the other way. While Mr. Powell wisely refused to be drawn into political analysis during his press conference, events this week point to an alternative path. Markets soared following Donald Trump's victory as investors anticipate lower taxes and deregulation. The lesson is that the right policies from Congress and the White House—or even the anticipation of such policies— can ease financial conditions by mobilizing capital for investment. *

Normal interest rates from the Fed can help by pushing that capital into more productive uses. This matters because the election delivered one mandate from voters above all others: to raise inflation-adjusted incomes for workers. Mr. Powell is risking political trouble for himself if persistent inflation above the Fed's target, or worse, an inflation rebound, makes that economic goal more difficult to achieve.

Mr. Powell said at his press conference Wednesday that he wouldn't resign if Mr. Trump asked him to before the end of his term in 2026. It would be unwise, and a waste of political capital, for Mr. Trump to ask him to. But Mr. Powell also doesn't want to have to raise rates early in Mr. Trump's second term to prevent an inflationary bounce back. *

Fed economists have a poor track record predicting how fiscal and regulatory policies will affect economic growth and inflation. This is a weakness as the Trump tax reforms, deregulation, fiscal gimmickry and tariffs constitute an unusually complex mix of policies. The Fed might do well to tread more carefully than it has in its recent meetings. *

