Economic Security Project Action

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Testimony before the House Financial Services Committee

Task Force on Monetary Policy, Treasury Market Resilience, and Economic Prosperity

“Examining Monetary Policy and Economic Opportunity”

March 4, 2025

Chairman Lucas, Ranking Member Vargas, and distinguished Members of the Task Force:

Thank you for inviting me to testify. My name is Mike Konczal, and I’m the Senior Director of Policy and Research at the Economic Security Project, where we advocate for ideas that build economic power for all Americans. Previously, I was a Special Assistant to the President and Chief Economist for the National Economic Council under President Biden, where I specialized in macroeconomic issues.

I applaud this Task Force investigating the importance of central bank independence and the dual mandate. Though the period following COVID was difficult, the United States had outcomes that far surpassed peer countries, and, as of late last year, the country was on a solid macroeconomic footing. There is always more to investigate and refine, but the core tools of balancing full employment and price stability outside short-term political pressures have served the country well.

I want to make three points today. First, the Federal Reserve was able to achieve the rare ‘soft landing’ of significantly bringing down the inflation that was driven by the global shocks of reopening with no cost to growth. Second, this achievement is now at risk due to the dangerous and irresponsible policy of the current administration, which will make high prices even more of a problem for everyday families. Finally, one of the most important macroeconomic decisions this year will be whether Congress increases the debt and deficit, putting pressure on the Fed and interest rates while raising the cost of mortgages and credit cards for families.

Soft Landing

First, there is a growing consensus that the global wave of inflation following the reopening was driven by multiple shocks.

Consumers radically shifted their spending from services to goods. Though overall real spending was on trend, this acted as a kind of cost-push shock, as the price of goods skyrocketed as people bought more, but the price of services did not fall. The shock to supply chains and commodities caused overall prices to rise, as businesses ran out of key inputs like semiconductors. This was made far worse when global commodity markets went into chaos following Russia's unprovoked invasion of Ukraine, especially for food and energy markets. Inflation peaked following that invasion, up to between 6 and 9 percent in the summer of 2022.

Professional forecasters and financial markets did not predict this inflation. The highest 10 forecasts for inflation compiled by Blue Chip in April 2021 averaged 2.7% for the following year, with the highest at 3.2%. The actual value was 8%.[1] This inflation was also global. Other countries saw inflation in the same range as the United States, even countries like Canada and Australia that had less direct exposure to Russian energy.

Many thought this inflation was driven by excessive demand and spending, requiring slower growth and higher unemployment for inflation to decline. Some believed unemployment would have to go to 10 percent; Bloomberg forecasted 100% chance of a recession in 2023.[2] But just as forecasters and markets missed inflation on the way up, they also missed it on the way down. Inflation fell between 3 and 6 percent, depending on the measurements, from its peak in early 2022 to the end of 2024.[3]

Meanwhile, we not only didn't have a recession, growth took off as inflation fell, pointing to the supply-side of the economy. Using contemporary macroeconomic tools, the 'sacrifice ratio,' or the amount GDP needs to fall to bring down inflation 1 point, for this disinflation was essentially 0, rather than the historically expected value well above 2. Over the last two years of the Biden administration, unemployment averaged below 4 percent and GDP growth was an annualized 2.9%, the former among the lowest values in 50 years and the latter well above the average of the 21st century.

As Ben Bernanke, the former Federal Reserve Chair and chairman of President George W. Bush's Council of Economic Advisers, recently said:

> "I think that the inflation was caused pretty much by the supply side [...] that it was most a supply shock. [...] This was primarily a supply shock inflation. The quantitative analysis suggests that the demand side factors were not strong enough [...] those of us who

[1] The Blue Chip Economic Indicators for April, 2021, full year over prior year, had CPI inflation at 2.2, 2.7, and 3.2 percent for average, top 10, and highest respectively in 2022. The actual value was 8 percent. The equivalent for PCE inflation was 2, 2.5, 2.8, and 6.6. For the 3-month treasury rate, it was 0.2, 0.3, 0.8, and 3 percent.

[2] Wingrove, J. (2022, October 17). *Forecast for US recession within year hits 100% in blow to Biden*. Bloomberg.

[3] Headline CPI, the prices consumers face, peaked at 8.6% year-over-year in the second quarter of 2022, and has since fallen 5.9% by the fourth quarter of 2024. Core PCE fell 2.8% from 5.6% in the first quarter of 2022 to 2.8%.

thought this was a supply side shock said, no, it'll be a pretty benign disinflation as the supply shocks unwind."[4]

The shock of the reopening and the subsequent price increases were difficult for working families. Real wages fell in 2021-2022 during the worst of the shocks, but began increasing again in 2023 and 2024. But, as the Economist magazine declared in late 2024, the US economy was "the envy of the world." Contrast with today, where reports describe a world of profound government policy uncertainty and CEOs worried about investing given their confusion as to what the basic rules of the road are going to be.[5]

Policy Uncertainty

Tariffs

That points us to the most immediate economic risk to inflation, the irresponsible policies of this current administration. I want to focus on three in particular: tariffs, weakened state capacity, and Federal Reserve independence.

Publicly announcing high tariffs outside formal process and in an inconsistent and confusing manner - where businesses go into a weekend uncertain what the actual North American trade law will be when they reopen on Monday - weakens growth and investment and makes consumers face higher prices. We are already seeing headlines about concerned CEOs and a striking decline in consumer sentiment, unanimous across age, income, and wealth groups.[6]

Normally, tariffs are small, strategic, and have little effect on aggregate prices. However, the tariffs currently under discussion are significantly higher and broader than past tariffs. One estimate from the Yale Budget Lab for the reciprocal tariffs being studied by the Commerce Department had prices rising "by 1.7-2.1%, the equivalent of an average per household consumer loss of $2,700 - 3,400" in a particularly regressive manner.[7]

The aggressive nature of this puts pressure on inflation expectations, as people and businesses start changing their behavior assuming higher prices are coming. The long-running University of Michigan survey found that "Inflation expectations over the next 5-10 years just rose to 3.5%, above expectations and the highest reading since April 1995" with consumers "fears that tariff-induced price increases are imminent."[8] Longer-term inflation expectations never slipped during

[4] American Economic Association. (2025, January 4). Inflation and the macroeconomy panel session. Panel video available here: https://www.aeaweb.org/webcasts/2025/inflation-macroeconomy
[5] The Economist. (2024, October 19). The American economy: The envy of the world. Special reports. Also, Hoffman, L., & Goswami, R. (2025, February 27). American business leaders are turning on Trump — fast. Semafor.
[6] University of Michigan. (2025, February 21). Consumer sentiment drops as inflation worries escalate.
[7] Yale Budget Lab. (2025, February 18). The fiscal, economic, and distributional effects of illustrative "reciprocal" US tariffs. Updated February 19, 2025.
[8] University of Michigan. (2025, February 21). Consumer sentiment drops as inflation worries escalate.

the reopening inflation as both the Biden administration and the Federal Reserve were committed to stopping price increases - the opposite of what we have here.

State Capacity

This is exacerbated by the attack on state capacity taking place during this administration, for example the government services being shut down and our private data being harvested by the DOGE committee. Cutting government waste and fraud is important, and Congress's own research services have found many ways in which that can be done. But this is not what is happening here.

This has two important macroeconomic impacts. In the long run it will weaken growth, as investments in research are randomly and haphazardly cut, and we lose our competitive edge in higher education and research.

But in the short run it will raise prices and reduce incomes for everyday people. Weakening consumer protection, allowing firms to rip off consumers with junk fees, raises prices. Forcing people to wait longer to address issues with Social Security payments because of disorderly layoffs is a de facto cut to Social Security. Reducing IRS capacity is a giant tax cut to billionaires who don't have to worry about playing by the rules.

Yet the state capacity issue is more subtle. We also dealt with avian flu outbreaks in the Biden administration, but we were able to work with government agencies such as the United States Department of Agriculture (USDA) to make sure information was being communicated clearly with the public, private markets, and food producers. Instead, now we see those agencies being dismantled and having their communications altered for ideological reasons, with severe cuts at USDA including those involved in managing bird flu.[9] According to government data, the retail price of a dozen eggs in January was $4.95, the highest on record and exceeding the peaks seen during commodity market turmoil or avian flu outbreaks under the Biden administration.[10]

Central Bank Independence

But the most dangerous item for macroeconomic policy is the removal of the independence of regulatory agencies through executive orders, threatening the independence of the central bank and of monetary policy.[11] Though the executive orders currently say that Federal Reserve monetary policy is exempted, that is an unstable arrangement, as politicization of other Federal Reserve functions and personnel will seep into monetary policy and central bank policy. Nothing

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[9] Smith, A., Zanona, M., & Strickler, L. (2025, February 18). USDA says it accidentally fired officials working on bird flu and is now trying to rehire them. NBC News.
[10] Federal Reserve Bank of St. Louis. (FRED). Average Price: Eggs, Grade A, Large (Cost per Dozen) in U.S. City Average. https://fred.stlouisfed.org/series/APU0000708111
[11] The White House. (2025, February 18). Ensuring accountability for all agencies: Executive order.

could destabilize an economy faster. The President sought to influence central bank actions during his first term; the threat of him doing so again would risk the overall economy.

Debt and Deficits

But ultimately the most important determinant for macroeconomics and the prices faced by people will be fiscal policy this year. And when it comes to that, the most important thing Congress will do is in handling the expiration of the Tax Cuts and Jobs Act (TCJA). And here, I also fear Congress will force everyday people to eat the costs of tax cuts for billionaires not just through massive cuts to health care and social insurance, but also through higher interest rates.

The TCJA could be extended only for everyday families to keep taxes low for them. However the extension of the tax cuts for those with high incomes and any additional tax cuts for the top on top of that will put pressure on spending at a time when the economy is near full employment. Previous unpaid Republican tax cuts were at times when there was more economic slack in the economy; now the end result will likely be higher interest rates for mortgages, credit cards, and loans with that extra level of spending.[12] Deficits under the House budget would average 6.8 percent of GDP per year over the next decade, a very high level given the low rates of unemployment.[13]

Worse, the exploding deficit caused by tax cuts will be used as a justification for painful cuts to health care and social insurance. Some estimates suggest that 36 million people are at risk of losing Medicaid due to likely Republican proposals aimed at covering the cost of tax cuts for billionaires.[14] Who is covered by Medicaid? That's 2 out of every 5 births and coverage for 2 out of every 5 children. That's the largest payer for mental health and long-term care services, with 3 out of 5 nursing facility residents.[15] And it is broader, as these cuts will put pressure on many rural hospitals that rely on Medicaid funding to stay open. Furthermore, in the event of a downturn, Medicaid and SNAP remain two of the few countercyclical programs available.

The overall plan of tariffs and spending cuts creates a potential for a cruel double whammy for working families: the proposed tariff package could skyrocket the cost of everyday goods, coupled with cuts to critical services as corporate tax breaks drain funding for public resources. Meanwhile, giant corporations getting these tax breaks can simply pass their costs on to consumers – protecting their profits while families struggle.

I look forward to taking your questions.

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[12] Bivens, J. (2025, February 13). There will be pain: Continuing low tax rates for the rich and corporations will hurt working families. Economic Policy Institute.
[13] Committee for a Responsible Federal Budget. (2025, February 21). House budget allows at least $2.8 trillion of deficit increases.
[14] Lukens, G., & Zhang, E. (2025, February 5). Medicaid work requirements could put 36 million people at risk of losing health coverage. Center on Budget and Policy Priorities.
[15] Orris, A., & Lukens, G. (2024, December 13). Medicaid threats in the upcoming Congress. Center on Budget and Policy Priorities.