The New York Times

Global central banks are focusing on inflation, but Omicron threatens

By Jeanna Smialek

December 6, 2021

A trio of the world's most important central banks took steps toward pulling back economic support this week as rapidly rising inflation burdens consumers and worries policymakers. But another threat hovered over those decisions: The new coronavirus variant Omicron.

Economists aren't yet sure what Omicron is going to mean for the global economy, but many are worried. Caseloads are rising rapidly in some places, and countries are already reacting by limiting travel. While the new strain of the virus seems less severe, the fact that it transmits so quickly could still lead to overwhelmed hospitals, analysts warn — and that is often the trigger for local economic shutdowns that toss people out of jobs and slow consumer spending.

Central banks are tracking that threat, but reacting to another reality: Inflation has taken off. Across advanced economies in Europe and in the United States, price gains have popped higher this year as tangled supply chains and goods shortages tied to the pandemic bite. Price pressures are lingering, and in the United States, proving broader than many had expected.

Still, some analysts questioned whether the course the Federal Reserve, Bank of England and European Central Bank are charting — one toward less economic support — would hold up in the face of another winter virus wave. It is a moment of vast uncertainty as policymakers move into inflation-fighting mode.

"The core issue is: We're dealing with many unusual and unfamiliar moving parts in the economy," said **Bernard Baumohl, chief global economist at the Economic Outlook Group.** "The dynamics are really complicated this time."

The Fed announced on Wednesday that it would slow down its bond purchases even more quickly that it had planned, which should position it to raise interest rates — its more traditional and powerful tool for cooling the economy — as soon as March, or shortly after. Officials estimated that they could raise rates three times next year.

The move completed a pivot for America's central bank, which had been cautiously backing away from supporting the economy, hoping to give the job market more time to heal.

"There's a real risk now, I believe, that inflation may be more persistent," Jerome H. Powell, the Fed chair, said at a news conference, later adding, "that's part of the reason behind our move today, is to put ourselves in a position to be able to deal with that risk."

Mr. Powell was also "quite blunt in asserting that the economy is strong enough to take faster tapering in its stride, no matter how bad" the Omicron wave is, Ian Shepherdson at Pantheon Macroeconomics wrote in a note responding to the meeting.

"We aren't quite so sure," he said. Mr. Shepherdson thinks that Omicron's infectiousness could make it a growth risk in the United States, but pointed out that the moment of "maximum economic danger" should come soon — so if the Fed is unable to stay the course on removing support, that would become clear quickly.

The Bank of England took an even more proactive inflation-fighting step Thursday, raising interest rates in a move that surprised analysts, giving Britain's ongoing Omicron surge.

"There was some value in waiting for further information on the degree to which Omicron was likely to escape the protection of current vaccines and on the initial economic effects of this new wave," minutes from the meeting acknowledged. "There was, however, also a strong case for tightening monetary policy now."

And the European Central Bank took a slower, more cautious step away from supporting the economy. It announced Thursday that it would slow and soon stop a pandemic-era bond buying program. But the central bank also said it would boost purchases in another program to smooth that transition and allow it to be flexible, given the uncertainty about the pandemic.

“Inflation is expected to remain elevated in the near term but should ease in the course of next year,” Christine Lagarde, head of the E.C.B., said at news conference after the decision. Policymakers also acknowledged the risk the virus posed in their statement announcing the change.

A question on many economists’ minds — and many policymakers’ — is what will happen if the pandemic hits growth but also lifts inflation. It could keep factories shut down, supply chains in disarray and workers at home, keeping goods and labor shortages rampant and inflation high.

“There’s a lot of uncertainty with the new variant and it’s not clear how big the effects would be on either inflation or growth or hiring,” Mr. Powell, the Fed chair, acknowledged Wednesday.

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