**Why the Fed Can’t Save Markets Right Now**

Taking a March rate increase off the table is easier said than done

Janet Yellen’s Federal Reserve is unlikely to raise rates in March.

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Investors are pretty much convinced that the Federal Reserve won’t be raising rates when it meets next month. Still, the central bank might do a lot to soothe global markets if it would just come out and say that.

But doing that may not be so simple.

Troubled emerging economies, falling commodity prices, global debt strains and a rising dollar have combined to create [a series of feedback loops](http://www.wsj.com/articles/fed-vs-the-dollar-why-yellen-cant-win-1454441168) that have rattled financial markets this year. The danger is that these will spill over into the U.S.

This would lower an inflation rate that the Fed already sees as too cool, and drag on growth. With policy makers, including Fed Governor Lael Brainard and Federal Reserve Bank of New York President [William Dudley](http://topics.wsj.com/person/D/William-Dudley/1046), lately [voicing caution on the outlook](http://www.wsj.com/articles/feds-brainard-makes-case-for-watchful-waiting-1454532865), futures markets are now implying just a 10% chance that the Fed raises rates at its March meeting.

Despite this, even the remote possibility that the Fed could still raise rates, represents a major tail risk—an unlikely event that, if it happens, could have very costly consequences.

So if Fed Chairwoman [Janet Yellen](http://topics.wsj.com/person/Y/Janet-Yellen/5513) at her semiannual Congressional testimony next week took a March tightening off the table, investors would breathe a lot easier. With the possibility of a major policy divergence between the Fed and the [Bank of Japan](http://quotes.wsj.com/JP/XTKS/8301) and European Central Bank nixed, for example, the dollar might give back more of its recent strength. That would take away some of the pain of global borrowers who are struggling to pay down dollar-denominated debt.

The catch: The market environment might then improve to the point that Fed policy makers could actually feel comfortable raising rates in March—especially if the intervening U.S. economic data looks decent. But the Fed, having taken that possibility off the table, could then feel constrained in its ability to do so.

More important, policy makers have spent the past year and more talking about how their decisions on rates will be “data dependent.” To clearly signal a policy hold an entire month before the March meeting would turn all the data-dependency talk into a farce.

So while the Fed might temporarily ease global market tensions with soothing words, it could also sow future problems.

In the end, the Fed will probably have to settle for so-called jawboning—sending strong hints through comments and speeches that a March rate increase isn’t coming. At the same time, officials won’t completely rule out the possibility that another rate increase may be in the offing.

It isn’t an ideal situation for either policy makers or investors. But it is probably the situation they are going to have to settle for.