Federal Reserve Chairman Janet Yellen pledged to maintain her predecessor’s policies by scaling back stimulus in “measured steps” and signaled that the bar is high for a change in that plan.

Only a “notable change in the outlook” for the economy would prompt policy makers to slow the pace of tapering, Yellen said in response to a question today during testimony to the House Financial Services Committee. “It’s important for us to take our time to assess” the significance of recent reports showing payrolls expanded less than projected, she said.

Stocks and Treasury yields climbed as Yellen, delivering her first public remarks as Fed chairman, said financial-market turmoil doesn’t pose a major risk to the outlook for the U.S. economy and repeated the Fed’s statement that asset purchases aren’t on a “pre-set course.”

The Taper in 90 Seconds

“Her message was continuity of policy and, matching that with continuity of outlook, suggests they remain on the same course,” said Keith Hembre, a former Minneapolis Fed researcher who helps oversee $125 billion as chief economist at Nuveen Asset Management LLC in Minneapolis.

The Standard & Poor’s 500 Index rallied 1.2 percent to 1,821.62 at 3:32 p.m. in New York. The yield on the 10-year note rose five basis points, or 0.05 percentage point, to 2.72 percent.

While growth has picked up, “the recovery in the labor market is far from complete,” Yellen said earlier in prepared remarks. “I am committed to achieving both parts of our dual mandate: helping the economy return to full employment and returning inflation to 2 percent while ensuring that it does not run persistently above or below that level.”

Asset Prices

Asset prices aren’t at “worrisome levels” even after the S&P 500 soared 30 percent last year, Yellen said, although the Fed is on the lookout for any threat of a bubble.

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“Our ability to detect bubbles is not perfect, but looking at a range of traditional valuation measures doesn’t suggest that asset prices broadly speaking are in bubble territory,” she said in response to a question.
The Fed chairman spoke days after a government report showed the jobless rate unexpectedly declined almost to the Fed’s threshold for considering an increase in the benchmark interest rate, even as payrolls growth cooled.

Yellen said the unemployment rate alone isn’t an adequate gauge of labor-market health.

Policy makers, who will see another jobs report before they next meet in March, “would be looking at a broad range of data on the labor market, including unemployment, job creation and many other indicators of labor market performance,” she said.

**Watching Volatility**

Yellen also said that the Fed has been “watching closely” volatility in global financial markets and that “our sense is that at this stage these developments do not pose a substantial risk to the U.S. economic outlook.”

In more than four hours of questioning, Yellen was pressed for her views on issues ranging from financial regulation and the budget deficit to coal prices and income inequality. She took care to avoid wading into partisan debates on subjects like the impact of the Affordable Care Act on the labor market.

In response to a question from Texas Democrat Ruben Hinojosa, Yellen said she’s troubled by growing income inequality.

“It’s one of the most important issues and one of the most disturbing trends facing the nation,” Yellen said. “Rising inequality is partly a matter of a weak job market that we are trying to address.”

**GAO Audits**

Yellen pushed back against Minnesota Republican Michele Bachmann’s assertion that Government Accountability Office audits of the Fed should be broadened to encompass monetary policy deliberations.

“Almost every aspect of our financial affairs” is already audited by the GAO, Yellen said. “What I don’t agree with and would strongly oppose is interfering with the independence of monetary policy by bringing political pressures to bear.”

Yellen, 67, used her testimony to praise her predecessor, Ben S. Bernanke, for helping “make our economy and financial system stronger” and said she’d continue his strategy.

“I expect a great deal of continuity in the FOMC’s approach to monetary policy,” Yellen said in her prepared remarks. She said she served on the Federal Open Market Committee “as we formulated our current policy strategy and I strongly support that strategy.”

**Asset Purchases**
The Fed said in December that it would start reducing the monthly pace of asset purchases, citing progress toward its goal of full employment. It announced a $10 billion reduction that month, followed by a cut of the same size in January, to $65 billion.

The central bank has said it will keep buying bonds until the outlook for the labor market has “improved substantially.”

Fed policy makers have also sought to reassure investors that while they are tapering bond purchases, they still intend to hold the Fed’s target rate near a record low.

Beginning in December 2012, the FOMC said it would keep the rate near zero “at least as long” as unemployment was above 6.5 percent. At the December 2013 meeting, it strengthened that statement, saying the rate is likely to stay near zero until “well past the time” unemployment falls below 6.5 percent, a strategy Yellen repeated today.

Unemployment in January fell to 6.6 percent, the lowest since October 2008, from 6.7 percent, a Labor Department report showed last week. Job growth in December and January was the weakest of any two-month period in the past three years.

Declining Unemployment

Joblessness has fallen faster than policy makers expected. When they first announced the threshold, most of them expected a rate of 7.4 percent to 7.7 percent at the end of 2013 and 6.8 percent to 7.3 percent at the end of this year.

Yellen took over as Fed chairman on Feb. 3 after serving for three years as Bernanke’s deputy. She has supported the bond purchases that expanded the Fed’s balance sheet to a record $4.1 trillion, and she helped craft a communications strategy designed to shape expectations for the future path of interest rates.

As vice chairman, Yellen also led a subcommittee that formalized the Fed’s goals for inflation and unemployment. The Fed now aims for inflation of 2 percent over the longer run. It has been undershooting that goal: the Fed’s preferred gauge of consumer prices climbed 1.1 percent last year.

Yellen hadn’t given detailed comments on the outlook for monetary policy and the economy since April, aside from her confirmation hearing in November. Outside of the confirmation process, she hadn’t testified before Congress as a central bank official since July 1996, when she was a Fed governor appointed by President Bill Clinton.

Target Rate

The Fed has held its target interest rate near zero since December 2008 and engaged in three rounds of bond buying. The easing policies helped push the S&P 500 up as much as 173 percent from a 12-year low in 2009.

The index is down about 1.4 percent this year, driven lower by turmoil in emerging markets and...
speculation about the direction of Fed policy. The MSCI Emerging Markets Index has lost 6.7 percent this year through yesterday.

“Investors appear to have been differentiating among” emerging market economies “based on their economic vulnerabilities,” according a Monetary Policy Report presented to the House committee. Brazil, India, Indonesia, South Africa, and Turkey are “among the economies that appear to have been the most affected” by the sell-off, according to the report.

Overall, “the degree of vulnerability across economies appears to be materially lower compared with past episodes,” because of more-flexible exchange rates and lower inflation.

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