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TRENDMACRO LIVE!

On the November FOMC

Thursday, November 8, 2018

Donald Luskin

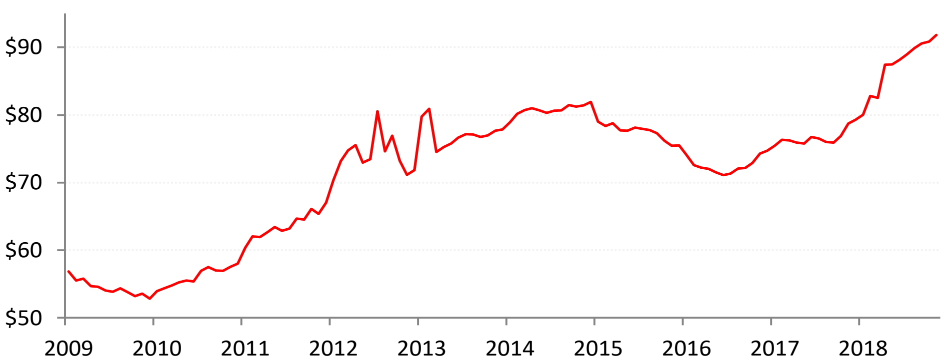
Noted: business fixed investment has slowed down. Perversely, this could mean tightening.

Well, the Powell Fed is making it easy for FOMC watchers. Statements get briefer and briefer, and there's never a dissent. Just about the most notable change in today's FOMC statement was the switch in time-zone from daylight savings time to standard time (see "Data Insights: Federal Reserve" September 26, 2018).

Almost. The statement language did note that "growth of business fixed investment…has moderated from its rapid pace earlier in the year." At the September meeting, it was said to "have grown strongly."

- Remember, this to us was a troubling disappointment in Q3-2018 GDP (see "Chinese Tariff Torture" October 29, 2018 and "Data Insights: GDP" October 26, 2018). For us, rising fixed investment is a sign that the corporate tax cuts are beginning to show their second-order – and sustainable – effects on growth by creating new incentives for firms to make capital expenditures.
- Happily, this fixed investment slowdown that nicked GDP – and that's surely where the FOMC is getting its information on this – is belied by consensus forward CAPEX per share for the S&P 500, which grew nicely in Q3 and continues to grow in Q4 (please see the chart below).
- New vice-chair Richard Clarida's speech last month touched on this – like us, he sees the link between investment growth and productivity growth. But like many old-school monetary

S&P 500 consensus forward CAPEX per share



Source: Bloomberg TrendMacro calculations

Update to strategic view

US FED, US MACRO: A brief statement in which the only major change was noting that "growth of business fixed investment…has moderated from its rapid pace earlier in the year." That troubles us to, because it throws the long-term effectiveness of corporate tax cuts into question – though forward CAPEX per share for the S&P 500 continues to grow rapidly. For the Fed, a drop in productivity growth, driven by a drop in investment growth, could fuel Phillips Curve cost-pressure fears unless wage growth drops too. This could fool the Fed into tightening just when the slackening of investment flow might be indicating that the Fed is already too tight.

[Strategy dashboard]

policymakers, for Clarida this otherwise correct insight leads down Phillips Curve rabbit-holes. Clarida presently sees no risk of inflation from "cost-push price pressure," because wages are only rising in pace with productivity – the rise of which he links to business fixed investment growth. *If fixed investment growth slackens off, and productivity growth slows – but if wages keep rising – Clarida could start thinking about tightening policy beyond gradual rates hikes in tune with the ongoing growth of the economy.*

- This is tortured pretzel-logic – by our lights, if anything, a fall-off in business fixed investment would more likely indicate that the Fed is already too tight, possibly having set rates too high for sufficient capital projects to produce forecasted rates of return above the hurdle rate. Thus any tightening under such conditions would be a double-error.
- By way of "on the other hand" economic logic, today's FOMC statement notes that household spending "has continued to grow strongly."
- Other than that, today's FOMC statement only noted that the unemployment rate "declined" – previously it had "stayed low." If you don't tell chair Jerome Powell that, in fact, the unemployment rate ticked *up* about half-a-percent at the last jobs report (see "On the October Jobs Report" November 2, 2018), we won't either.
- That was easy.

Bottom line

A brief statement in which the only major change was noting that "growth of business fixed investment…has moderated from its rapid pace earlier in the year." That troubles us to, because it throws the long-term effectiveness of corporate tax cuts into question – though forward CAPEX per share for the S&P 500 continues to grow rapidly. For the Fed, a drop in productivity growth, driven by a drop in investment growth, could fuel Phillips Curve cost-pressure fears unless wage growth drops too. This could fool the Fed into tightening just when the slackening of investment flow might be indicating that the Fed is already too tight.

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