TrendMacro

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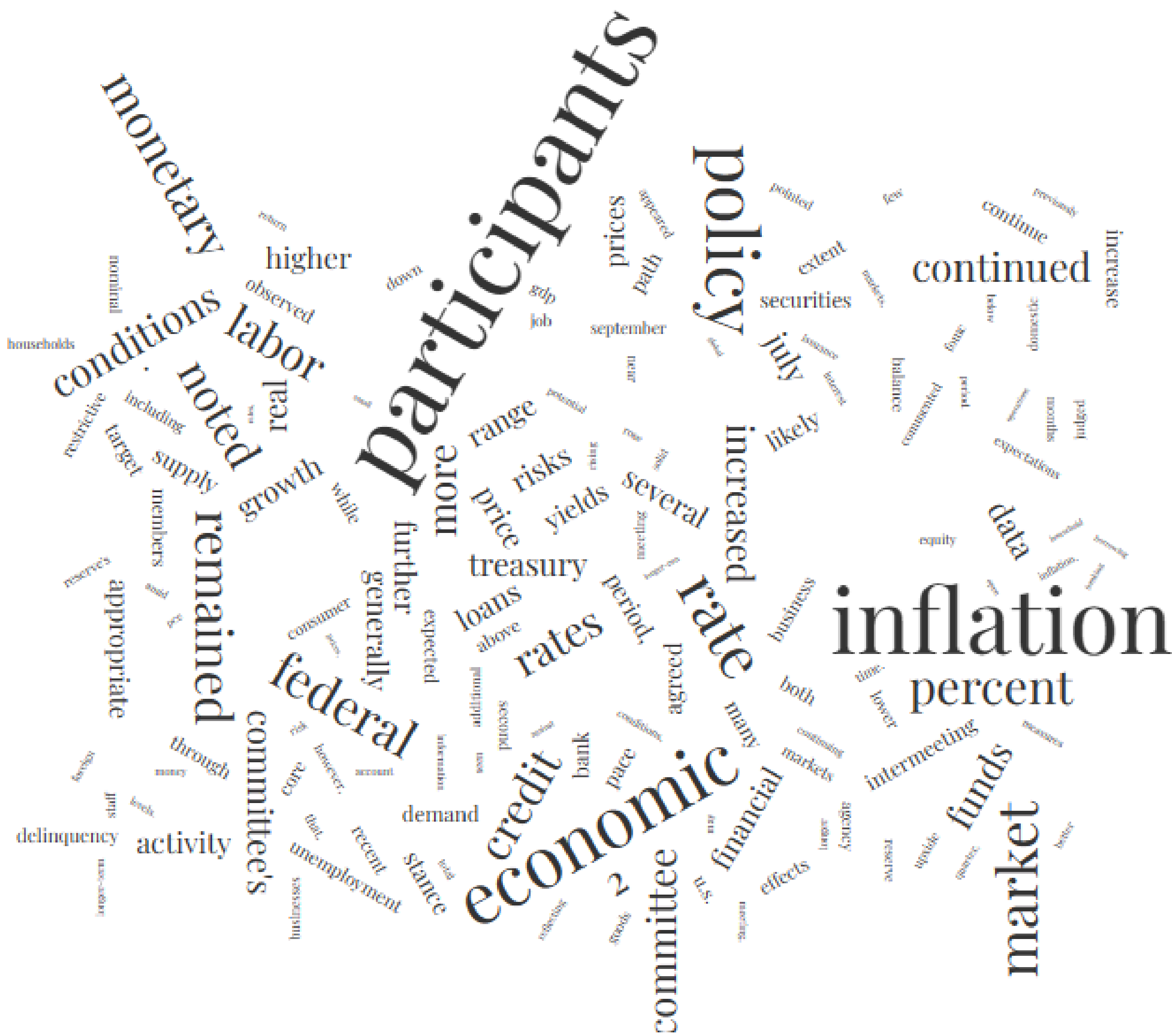
Data Insights: FOMC Minutes

Wednesday, October 11, 2023

September minutes   Key signaling language: Featured   Important   Very important



…In addressing the increase in nominal yields on longer-run Treasury securities over the intermeeting period, the manager noted that the rise in real yields exceeded that of nominal yields over the period, implying a small decline in inflation compensation.

Inflation expectations appeared to remain very well anchored. Market participants cited various factors for the rise in longer-term nominal yields, including stronger-than-expected economic data, a possible increase in the neutral policy rate, greater economic and policy uncertainty, and larger-than-expected borrowing by the Treasury.

…The imbalance between labor demand and supply appeared to be easing. Total nonfarm payroll employment increased at a slower pace over July and August than in the second quarter. The private-sector job openings rate and the quits rate, both measured by the Job Openings and Labor Turnover Survey, moved down further through July. Over July and August, the unemployment rate edged up, on net, and stood at 3.8 percent in August, and both the labor force participation rate (LFPR) and the employment-to-population ratio rose slightly. The unemployment rate for African Americans declined, while the jobless rate for Hispanics rose, and both rates were still above the national average. The easing of labor market imbalances was also evident in the recent wage data, with the 12-month changes in average hourly earnings and the employment cost index, and the four-quarter change in business-sector compensation per hour all lower than their year-earlier levels.

Consumer price inflation remained elevated but continued to show signs of slowing. The total price index for personal consumption expenditures (PCE) increased 3.3 percent over the 12 months ending in July, and core PCE price inflation, which excludes changes in energy prices and many consumer food prices, was 4.2 percent over the same period; both total and core PCE price inflation were lower than a year earlier. The trimmed mean measure of 12-month PCE price inflation constructed by the Federal Reserve Bank of Dallas was 4.1 percent in July, down from its level earlier in the year. In August, the 12 month change in the consumer price index (CPI) was 3.7 percent, while core CPI inflation was 4.3 percent over the same period, and both total and core CPI inflation were well below their year-earlier levels. Survey measures of consumers' short-term inflation expectations had moved down alongside actual inflation but remained above pre-pandemic levels. In contrast, survey measures of medium- to longer-term inflation expectations remained in the range seen in the decade before the pandemic.

…Bank credit conditions appeared to tighten somewhat over the intermeeting period, but credit to businesses and households remained generally accessible. Commercial and industrial loan balances contracted, but outstanding commercial real estate (CRE) loans increased from July through late August, though at a slower pace than earlier in the year. Within the category of CRE loans, nonfarm nonresidential loans contracted over the summer for the first time since March 2022. Bank funding conditions were generally stable. Core deposits declined but were offset by inflows of large time deposits.

…Credit quality deteriorated a little further across many sectors in recent months but remained broadly solid. In the CRE sector, delinquency rates on nonfarm nonresidential CRE bank loans rose over the second quarter, while delinquency rates on construction, land development, and multifamily loans were roughly unchanged. Delinquency rates of loans in CMBS pools increased, driven by the office and retail sectors. The office delinquency rate rose more than 2 percentage points since January but remained below its pre-pandemic average. The delinquency rate for small business loans ticked up in June and July. Delinquency rates for credit cards and auto loans increased further in the second quarter and stood a bit above their average levels in the years leading up to the pandemic. The fraction of potential borrowers with a prime credit score expanded through the second quarter, moving further above its pre-pandemic level. The trailing default rates for investment- and speculative-grade corporate bonds increased in July but remained at historically low levels. The trailing default rate for leveraged loans was little changed, on net, but downgrades of leveraged loans surpassed upgrades in July and August.

In contrast to many other types of loans, the payment performance of home mortgages improved. Delinquency rates of Federal Housing Administration and Department of Veterans Affairs loans in July were lower than levels seen earlier this year, and delinquency rates of conventional loans remained at historical lows. Credit quality was also strong for municipal borrowers.

… A Summary of Economic Projections (SEP) was released to the public following the conclusion of the meeting.

Regarding the economic outlook, participants assessed that real GDP had been expanding at a solid pace and had been more resilient than expected. Nevertheless, participants also noted that they expected that real GDP growth would slow in the near term. Participants judged that the current stance of monetary policy was restrictive and that it broadly appeared to be restraining the economy as intended. Participants stressed that current inflation remained unacceptably high while acknowledging that it had moderated somewhat over the past year. They also noted that further evidence would be required for them to be confident that inflation was clearly on a path to the Committee's 2 percent objective. Participants continued to view a period of below-trend growth in real GDP and some softening in labor market conditions as likely to be needed to bring aggregate demand and aggregate supply into better balance and reduce inflation pressures sufficiently to return inflation to 2 percent over time.

In their discussion of the household sector, participants observed that aggregate consumer spending had continued to exhibit considerable strength, supported by the strong labor market and by generally strong household balance sheets. However, many participants remarked that the finances of some households were coming under pressure amid high inflation and declining savings and that there had been an increasing reliance on credit to finance expenditures. In addition, tighter credit conditions, waning fiscal support for families, and a resumption of student loan payments were viewed by several participants as having the potential to weigh on the growth of consumption. While household credit quality was seen as generally strong, a few participants noted rising delinquency rates on some types of consumer credit. A couple of participants also remarked that households were becoming increasingly price sensitive. Some participants noted that housing demand was resilient despite higher interest rates; new home construction was solid, in part reflecting the limited inventory of homes available for sale.

Regarding the business sector, participants noted that activity continued to be solid, though several pointed to signs of softening conditions. Many participants noted improved business conditions from an increased ability to hire and retain workers, better-functioning supply chains, or reduced input cost pressures. A few participants commented that their business contacts had reported difficulties passing on cost increases to customers. Several participants judged that, over coming quarters, business activity would be restrained by tighter financial conditions, such as higher interest rates and more constrained access to bank credit. Several participants noted, however, that the tightening of credit conditions resulting from the banking stresses earlier in the year was likely to be less severe than they previously expected. A number of participants expressed concerns about vulnerabilities in the CRE sector. Many participants commented that they expected that the autoworkers' strike would, in the near term, result in a slowdown in production of motor vehicles and parts and possibly put upward pressure on automobile prices, but that these effects would be temporary. With respect to the agricultural sector, a few participants noted that conditions were mixed, as crop prices had declined amid higher production estimates and as supply and demand imbalances pushed up the prices of some types of livestock and held down the prices of others.

Participants observed that the labor market was tight but that supply and demand conditions were continuing to come into better balance. Most participants remarked that a range of indicators of labor demand were easing—as could be seen by declines in job openings, a narrowing of the jobs-to-workers gap, lower quits rates, and a reduction in average weekly hours worked to levels at or below those seen before the pandemic. However, several participants noted that labor markets remained very tight in some sectors of the economy, such as health-care services and education. Many participants also observed that measures of labor supply, especially the LFPR, had moved up. Some participants commented that the increase in the LFPR for women had been particularly notable, although they expressed concern that challenges regarding the availability of childcare could affect the sustainability of this increase in participation. Several participants noted that immigration had also been boosting labor supply. Some participants observed that payroll growth remained strong but had slowed in recent months to a pace closer to that consistent with maintaining a constant unemployment rate over time. Most participants commented that the pace of nominal wage increases had moderated, and a few also mentioned that the wage premium for job switchers had come down. They noted, however, that nominal wages were still rising at rates above levels generally assessed to be consistent with the sustained achievement of the Committee's 2 percent inflation objective, given current estimates of trend productivity growth.

Participants noted that the data received over the past several months generally suggested that inflation was slowing. Even with these favorable developments, they emphasized that further progress was needed to get inflation sustainably to 2 percent. Participants pointed to the softening of price inflation for goods amid improving supply conditions and to declining housing services inflation. Several participants remarked that, despite the recent rise in energy prices, food and energy prices over the past year had contributed to a decline in overall inflation. However, participants also noted that significant progress in reducing inflation had yet to become apparent in the prices of core services excluding housing. Participants noted that longer-term inflation expectations remained well anchored and that shorter-term inflation expectations had been moving down from elevated levels. Participants observed that, notwithstanding recent favorable developments, inflation remained well above the Committee's 2 percent longer-run objective and that elevated inflation was continuing to harm businesses and households—particularly low-income households. Participants stressed that they would need to see more data indicating that inflation pressures were abating to be more confident that inflation was on course to return to 2 percent over time.

Participants generally noted there was still a high degree of uncertainty surrounding the economic outlook. One new source of uncertainty was that associated with the autoworkers' strike, and many participants observed that an intensification of the strike posed both an upside risk to inflation and a downside risk to activity. A majority of participants pointed to upside risks to inflation from rising energy prices that could undo some of the recent disinflation or to the risk that inflation would prove more persistent than expected. Various participants noted downside risks to economic activity, including that credit conditions might tighten more than expected if the domestic banking sector experienced further strains; the possibility that the economic slowdown in China could result in a drag on global economic growth; or that an extended U.S. government shutdown could have negative, albeit temporary, consequences for growth. Some participants remarked that an upside risk to their projections for economic activity was that the unexpected resilience that the economy had demonstrated so far could persist. Several participants commented that a government shutdown might result in the delayed release of some economic data and that this outcome would make it more difficult to assess economic conditions. A few participants observed that there were challenges in assessing the state of the economy because some data continued to be volatile and subject to large revisions.

In their consideration of appropriate monetary policy actions at this meeting, participants concurred that economic activity had been expanding at a solid pace and had been resilient. While the labor market remained tight, job gains had slowed, and there were continuing signs that supply and demand in the labor market were coming into better balance. Participants also noted that tighter credit conditions facing households and businesses were a source of headwinds for the economy and would likely weigh on economic activity, hiring, and inflation. However, the extent of these effects remained uncertain. Although inflation had moderated since the middle of last year, it remained well above the Committee's longer-run goal of 2 percent, and participants remained resolute in their commitment to bring inflation down to the Committee's 2 percent objective. Amid these economic conditions, and in consideration of the significant cumulative tightening in the stance of monetary policy and the lags with which policy affects economic activity and inflation, almost all participants judged it appropriate to maintain the target range for the federal funds rate at 5-1/4 to 5-1/2 percent at this meeting. Participants judged that maintaining this restrictive stance of policy would support further progress toward the Committee's goals while allowing the Committee time to gather additional data to evaluate this progress. All participants agreed that it was appropriate to continue the process of reducing the Federal Reserve's securities holdings, as described in its previously announced Plans for Reducing the Size of the Federal Reserve's Balance Sheet.

In discussing the policy outlook, participants continued to judge that it was critical that the stance of monetary policy be kept sufficiently restrictive to return inflation to the Committee's 2 percent objective over time. A majority of participants judged that one more increase in the target federal funds rate at a future meeting would likely be appropriate, while some judged it likely that no further increases would be warranted. All participants agreed that the Committee was in a position to proceed carefully and that policy decisions at every meeting would continue to be based on the totality of incoming information and its implications for the economic outlook as well as the balance of risks. Participants expected that the data arriving in coming months would help clarify the extent to which the disinflation process was continuing and labor markets were reaching a better balance between demand and supply. This information would be valuable in determining the extent of additional policy firming that may be appropriate to return inflation to 2 percent over time. Some participants also emphasized the importance of continuing to communicate clearly to the public about the Committee's data-dependent approach to policy and its firm commitment to bring inflation down to 2 percent.

All participants agreed that policy should remain restrictive for some time until the Committee is confident that inflation is moving down sustainably toward its objective. A few participants noted that the pace at which inflation was returning to the Committee's 2 percent goal would influence their views of the sufficiently restrictive level of the policy rate and how long to keep policy restrictive. Several participants commented that, with the policy rate likely at or near its peak, the focus of monetary policy decisions and communications should shift from how high to raise the policy rate to how long to hold the policy rate at restrictive levels. A few participants noted that it would be important to monitor the real federal funds rate in gauging the stance of monetary policy over time. Most participants observed that postmeeting communications, including the SEP, would help clarify to the public how participants assessed the likely evolution of the stance of monetary policy. Participants observed that the continuing process of reducing the size of the Federal Reserve's balance sheet was an important part of the overall approach to achieving their macroeconomic objectives. Several participants noted that the process of balance sheet runoff could continue for some time, even after the Committee begins to reduce the target range for the federal funds rate.

A vast majority of participants continued to judge the future path of the economy as highly uncertain. Many noted data volatility and potential data revisions, or the difficulty of estimating the neutral policy rate, as supporting the case for proceeding carefully in determining the extent of additional policy firming that may be appropriate.

Participants discussed several risk-management considerations that could bear on future policy decisions. Participants generally judged that, with the stance of monetary policy in restrictive territory, risks to the achievement of the Committee's goals had become more two sided. But with inflation still well above the Committee's longer-run goal and the labor market remaining tight, most participants continued to see upside risks to inflation. These risks included the imbalance of aggregate demand and supply persisting longer than expected, as well as risks emanating from global oil markets, the potential for upside shocks to food prices, the effects of a strong housing market on shelter inflation, and the potential for more limited declines in goods prices. Many participants commented that even though economic activity had been resilient and the labor market had remained strong, there continued to be downside risks to economic activity and upside risks to the unemployment rate. Such risks included larger-than-anticipated lagged macroeconomic effects from the tightening in financial conditions, the effect of labor union strikes, slowing global growth, and continued weakness in the CRE sector. Participants generally noted that it was important to balance the risk of overtightening against the risk of insufficient tightening.

Source: Federal Reserve Board