

TRENDMACRO LIVE!

On the July FOMC, and Cohn for Fed Chair?

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Donald Luskin

We still say Yellen, if she wants it. At least Trump is looking away from tight-money zealots.

Many clients have asked us this week for our views on whom President Trump will appoint as Fed Chair when Janet Yellen's term expires in February. The questions are in the manner of looking for downside risks in the face of stocks melting up to new highs world-wide, and risk premia of all kinds narrowing. In response, *we reiterate our longstanding view that incumbent chair Yellen is the front-runner* (see ["Yellen Gives Conservatives Something to Cheer"](#) February 17, 2017).

- *We see that steady-as-she-goes choice as the one most likely to sustain the present favorable macro environment.* Despite our deep initial reservations (see ["On Yellen for Fed Chair"](#) October 9, 2013), we think Yellen has done a fine job and is on the right track (see ["Yellen's March to Neutrality"](#) March 6, 2017).

We have not seen National Economic Council director Gary Cohn as an especially likely candidate, but perhaps he needs to be upgraded in light of remarks by Trump in [an interview yesterday with the Wall Street Journal](#).

- *He hasn't accomplished much for Trump in his current position, so far. So why a promotion?*
- Reports of Cohn as a Fed chair candidate [began in late May](#), in a way that struck us as particularly unsourced and gossip-driven. [Subsequent reports](#) strike not as corroboration, but as likely re-reports – that is, echoes – of the initial one.
- In yesterday's *Journal* interview, Cohn's name came up in the context of a discussion about Yellen, and only because Trump was specifically asked – another echo. Trump said, "I've known Gary for a long time, but I've gained great respect for Gary working with him... So Gary certainly would be in the mix... He doesn't know this, but yes."
- Okay, so Cohn can no longer easily be dismissed as a possibility. But he's hardly "the top contender" as [claimed in overheated headlines today](#). That title still goes to Yellen.
- Cohn was [in the room](#) during the interview. Even Trump would have to be somewhat diplomatic. Even at that, Trump said, "I actually think he likes what he's doing right now."

Update to strategic view

US FED, US MACRO, US BONDS: In an interview yesterday Trump talked up Yellen for re-appointment but, when asked, did not rule out Cohn. As chair Cohn would be an uncertainty factor, as almost nothing is known about his monetary policy philosophy. Trump's praise for Yellen is based on her demonstrated philosophy as Trump sees it, including a bias toward low interest rates and distrust of a too-strong dollar. Trump's preference for such biases would rule out perma-hawk Goodfriend. Yellen has been particularly unclear about whether she would accept re-appointment. No surprises in the FOMC statement. Labor market strength was slightly upgraded, and progress on inflation was somewhat downgraded – a combination that will disappoint any remaining Phillips Curve believers. Non-reinvestment of Treasuries and MBS is now said to start "relatively soon." We think the announcement will come at the September FOMC. With inflation faltering and the balance sheet unwind beginning, there will be no more rate hikes in 2017.

[\[Strategy dashboard\]](#)

- We have no basis at this moment for a strong opinion on what Cohn would be like as a Fed Chair. He has no history with the institution or the ideas that animate it, unlike Yellen or Ben Bernanke – both of whom were very much knowable and known quantities when they became chair. *Cohn would be an uncertainly-factor as chair – but, truth be told, they all are, no matter their seeming track records, given the unpredictable challenges they all eventually face.*
- The most intriguing possibility would be for Trump to nominate Cohn for chair, and then call back Bernanke’s vice chair to replace Stanley Fisher at the end of his term in mid-2018. Then the Federal Reserve would be chaired and vice chaired by Cohn and Kohn.

As to Yellen, her reappointment requires both that Trump wants her, and that she wants the job. Under questioning about it two weeks ago in connection with her [Semi-Annual Monetary Policy Report to the Congress](#), it struck us that she fumbled around a bit with her answer. She told the House, “I really haven’t had to give further thought at this point to this question.” When asked in the Senate, at first, she said only, “Excuse me?” Then when asked again, she said, “I... haven’t really decided that issue.” At age 70, she is not necessarily in the best of health. [At a speech in late 2015](#), she experienced what [appeared to be an aphasic episode](#). Several weeks ago [she was hospitalized](#) for a urinary tract infection.

- Perhaps she’s legitimately undecided about her own wishes. Perhaps she, [a Yale liberal](#) married to [a Yale liberal](#), is inclined to feel she was especially poorly treated by Trump during the presidential campaign, and doesn’t want to have to deal with him.
- Candidate Trump [accused Yellen](#) of keeping rates low “because she’s obviously political and doing what Obama wants her to do... it’s a false market. Money is essentially free.” Yellen “should be ashamed of herself.”
- But once in office, [Trump said](#) that Yellen is “not toast... I like her, I respect her.”
- In [yesterday’s Journal interview](#), Trump said:

“I have a lot of respect for her, and I like her. I’ve met her just a couple of times, but I like her. It’s early to make the decision... I do like low interest rates. I mean, you know, I’m not making that a big secret. I think low interest rates are good. I like a dollar that’s not too strong. I mean, I’ve seen strong dollars. And frankly, other than the fact that it sounds good, lots of bad things happen with a strong dollar. ... I would say yes, she is in the running to stay... It’s very early... But she is – she is in the running, absolutely. I like her. I like her demeanor. I think she’s done a good job. I’d like to see rates stay low. She’s always been – you know, she’s historically been a low-interest-rate person, a believer.”

The key in all this is not so much the person of Janet Yellen or Gary Cohn, but the philosophical framework in which Trump will choose his appointee. *The biggest risk is that, perhaps more out of loyalty to GOP shibboleths*

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On the web at
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Donald Luskin
Chicago IL
312 273 6766
don@trendmacro.com

Thomas Demas
Charlotte NC
704 552 3625
tdemas@trendmacro.com

Michael Warren
Houston TX
713 893 1377
mike@trendmacro.energy

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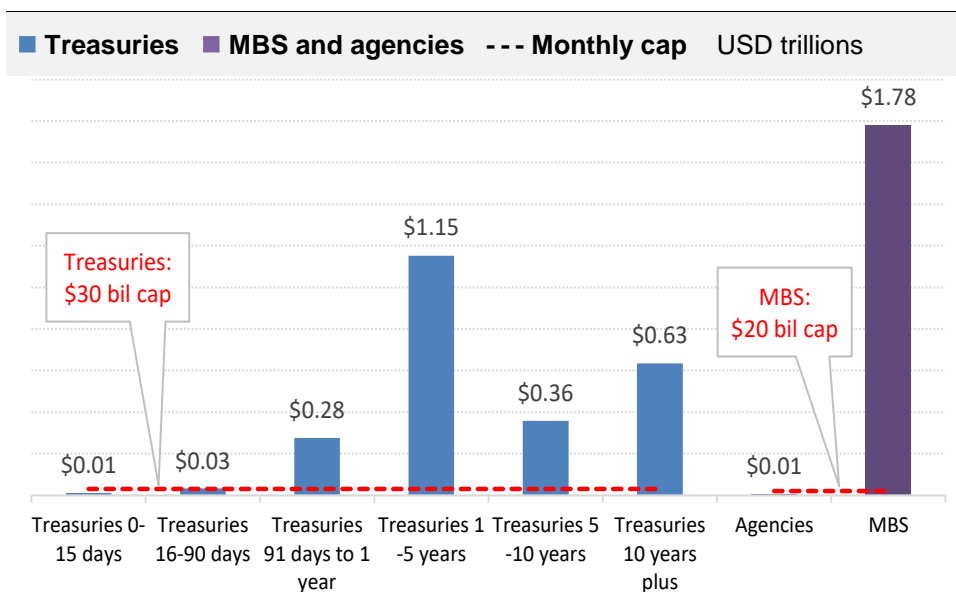
than any personal belief system, Trump might nominate a rock-ribbed permahawk dedicated to some nostalgic idea of “normal” monetary policy, or wedded to “policy rules” calibrated in a bygone economic era.

- One such person is Marvin Goodfriend, whom we warned was strongly rumored to be under consideration as a nominee for Federal Reserve Board Governor, which could be a stepping-stone to the chair, as it was for both Bernanke and Yellen (see [“Trump’s New Faces on the Fed”](#) June 5, 2017).
- So far Trump has not placed Goodfriend’s name before the Senate. Meanwhile, while Randal Quarles, who was rumored for FRB governor at the same time early last month – as vice chair for bank supervision, replacing Daniel Tarullo – has been [officially nominated](#).
- If Trump is sincere in his statements yesterday to the *Journal* – celebrating low interest rates, and dismissing a strong dollar as an unalloyed good – then Goodfriend ought to be seen as out of the running, at least for chair.
- If true, that’s the best possible answer to client concerns about Yellen’s re-appointment or replacement. The chairmanship of the Federal Reserve is an impossible job and everyone who assumes it will err one way or another. But the last thing the global economy needs is a tight-money zealot, and for now, that seems to be off the table.

Oh. We almost forgot. There was an FOMC meeting today.

- As universally expected, the FOMC left policy rates unchanged.
- [Today’s FOMC statement](#) differed hardly at all from [June’s](#) (see [“Data Insights: Federal Reserve”](#) July 26, 2017).
- Job gains are now characterized as having been “...solid, on average, since the beginning of the year.” Hard to really know what it even means for a time series to be “solid, on average” when it has varied so much from month to month – that variance would seem to be evidence of lack of solidity. No matter to this FOMC. June’s upside surprise in net payrolls (see [“On the June Jobs Report”](#) July 7, 2017) was enough to remove the last meeting’s observation that jobs gains have “moderated.”
- On a more cautious note, inflation, both headline and core, are now confessed to be “running below 2 percent,” as opposed to last meeting’s more hopeful “somewhat below.”
- If there’s anyone on the Fed who still believes in the Phillips Curve, this should be sobering – inflation isn’t supposed to be weakening when the labor market is strengthening. Oh well...
- The onset of non-reinvestment of maturities in the Fed’s Treasury and MBS portfolio is now said to be expected “relatively soon.” The last meeting’s statement had said only “this year.”
- “Relatively soon” probably means it will be announced at the September FOMC, with implementation beginning in October. This is not unexpected by the markets.

- This, too, has been a topic of great interest in client conversations this week. We continue to believe it will be a non-event for markets and the economy (see [“Time for Taper Tantrum Two?”](#) April 6, 2017).
- There will be no critical cash-call for markets as the Fed ceases to reinvest, because all the money the private sector needs to take up the slack is sitting on the Fed’s balance sheet, primarily in the form of “excess reserves.”
- And we think at this point, with risk premia of all types at multi-year or even historic lows, there is plenty of absorption capacity for the duration and pre-payment risk that will slowly creep back into the market.
- We do mean *slowly*. The pace of non-reinvestment will run, even when it gets up to full speed where it will be capped at \$50 per month, at only about \$1 billion per calendar day – because the monthly cap will only occasionally be hit (please see the chart below, and [“On the June FOMC”](#) June 14, 2017).



Source: FRB, TrendMacro calculations

- All that said, out of an abundance of caution we think the Fed is unlikely to raise rates again this calendar year, while the onset of balance sheet unwinding is still new and uncertain. With inflation faltering, this shouldn’t even be a close call.

Bottom line

In an interview yesterday Trump talked up Yellen for re-appointment but, when asked, did not rule out Cohn. As chair Cohn would be an uncertainty factor, as almost nothing is known about his monetary policy philosophy. Trump’s praise for Yellen is based on her demonstrated philosophy as Trump sees it, including a bias toward low interest rates and distrust of a too-strong dollar. Trump’s preference for such biases would rule out perma-hawk Goodfriend. Yellen has been particularly unclear about

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