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TRENDMACRO LIVE!

On the June FOMC

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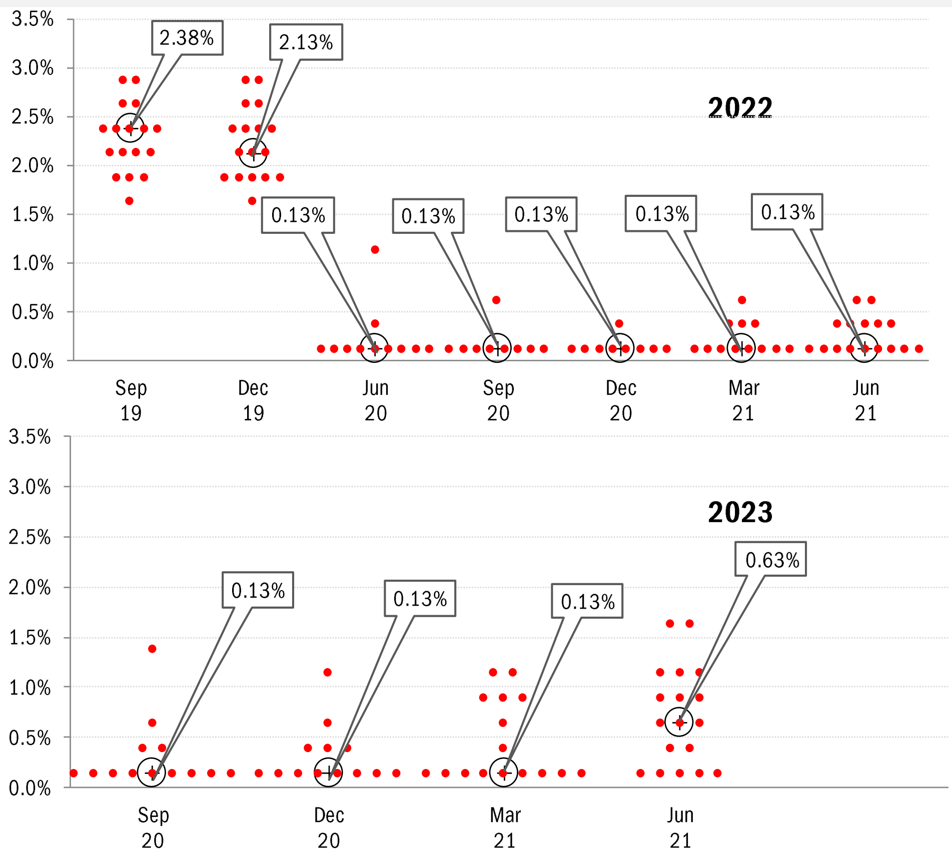
Did the FOMC just say the economy will grow faster without massive new federal spending?

We have sensed among clients an air of dread about this FOMC meeting. There has been a broad consensus that the "dots" in the Summary of Economic Projections would be moved up to indicate consensus for lift-off in 2023 from the present near-zero funds rate. *The median of the 2023 dots calls for two rate hikes in 2023, up from none at all in the March SEP. Just three dots out of 18 migrated in favor of one hike in 2022, but the median remains firmly anchored at none* (please see the chart below).

- *So the air of dread was prescient, but that only means the shift in the 2023 dots is no surprise, and ought not to move markets*

Estimated appropriate funds rate in SEP, by FOMC meeting ● Participant ○ Median



Source: Federal Reserve Board, TrendMacro calculations

Update to strategic view

US FED, US MACRO, US BONDS: The 2023 "dots" now forecast two rate hikes, up from zero forecasted in May. But this only matches expectations already embedded in forward prices. The SEP upgraded expectations for growth, unemployment and inflation. It's something of an embarrassment that the forecasted real GDP growth rate for 2023, without assuming the White House's massive spending proposals, is higher than the White House's own forecast that does assume them – implying the economy is better off with them. Moreover, Powell admitted that unemployed persons will seek work when enhanced unemployment benefits run off, suggesting that the benefits were a policy error. Neither help Powell's re-appointment prospects. Powell finessed the question of tapering, moving past the "talking about talking about" trope. Yields should move higher regardless in virtue of improving growth. Inflation was not intensely questioned in the presser, anecdotal evidence that self-fulfilling expectations are anchored.

[Strategy dashboard]

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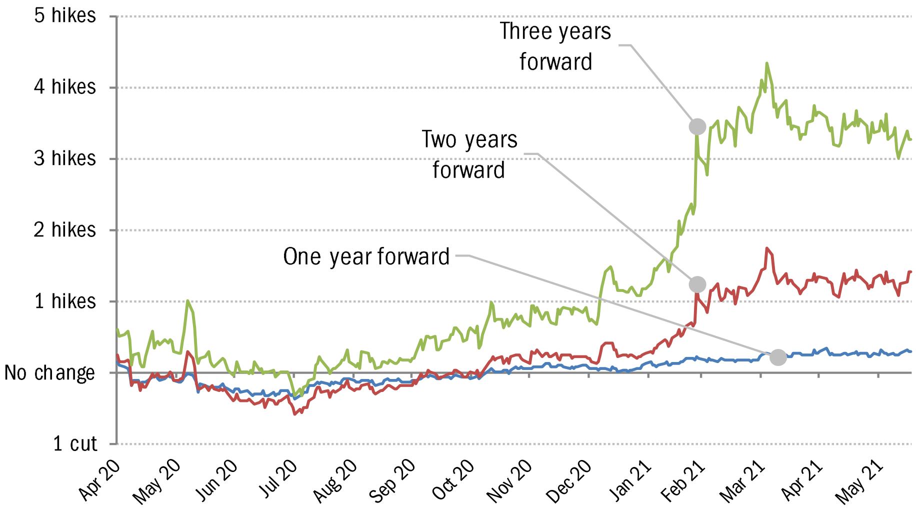
much. Indeed, the two hikes in 2023 have been pretty much embedded in the money-market curve already for months (please see the chart below).

Market-implied forward number of 25 bp rate hikes



Source: Bloomberg, TrendMacro calculations

- *Moreover, we can't emphasize enough that the prospect of lift-off from the zero-bound is a constructive manifestation of improving growth and growth expectations*.
- In the SEP, the median forecasts for real GDP growth, unemployment and inflation all improved (please see the charts on the following page). Moreover, in the SEP's disclosure of the direction of uncertainty around the Committee's forecasts, in all cases the dominant risk is now seen as that of not being optimistic enough (see "Data Insights: Federal Reserve" June 16, 2021).
- *We note with particular emphasis that in the post-meeting press conference, chair Jerome Powell opined that the roll-off of enhanced unemployment benefits would motivate some unemployed workers to seek a job. No doubt thinking about his re-appointment as chair coming up, he didn't outright say that it was a policy error to pay people more not to work than to work. But that was his point.*
- *We also note that the SEP median expectation for real GDP growth in 2023 is now 2.4%, upgraded from 2.2% in March. Presumably this expectation does not embed any of the large spending programs proposed in the White House's fiscal 2022 budget. Yet the White House's growth forecast for 2023, which surely does include them, calls for only 2.2%. If Powell wants to get reappointed, it's not helpful that the FOMC as a body appears to believe that the economy will have faster growth in 2023 without the White House's program.*

There has also been fear that Chair Jerome Powell will set off a tantrum by signaling tapering asset purchases by saying the FOMC is talking about talking about it at a coming meeting. But the reality is that, according to the

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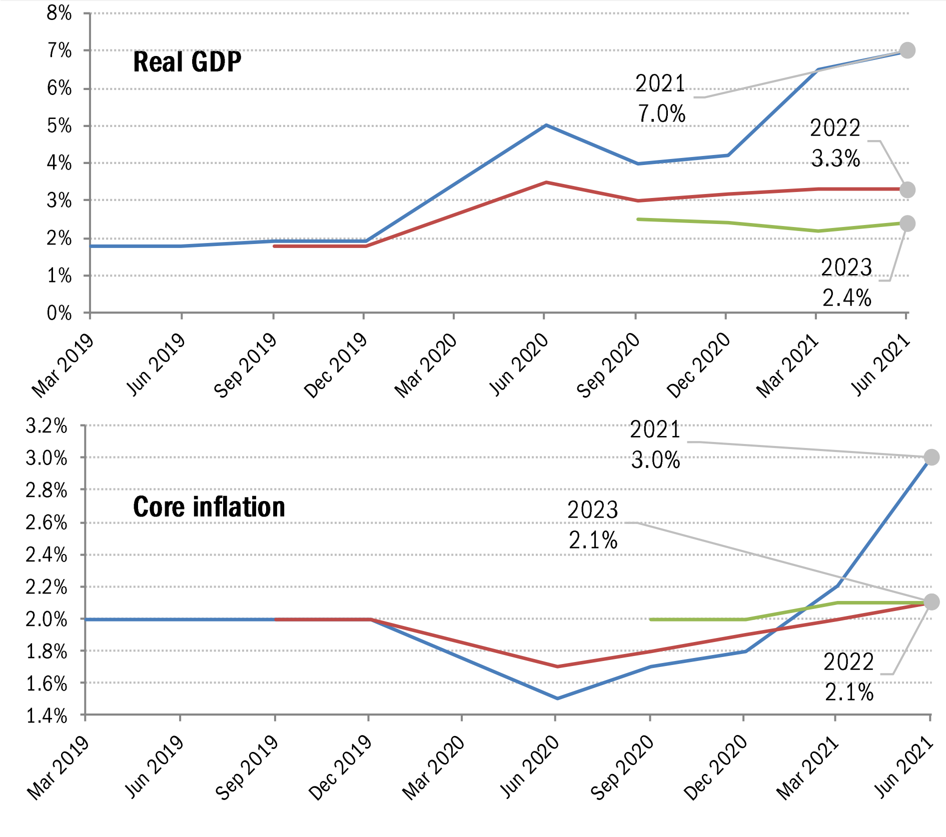
[About us]

FOMC participants' estimate of growth and inflation in [SEP](), by FOMC meeting



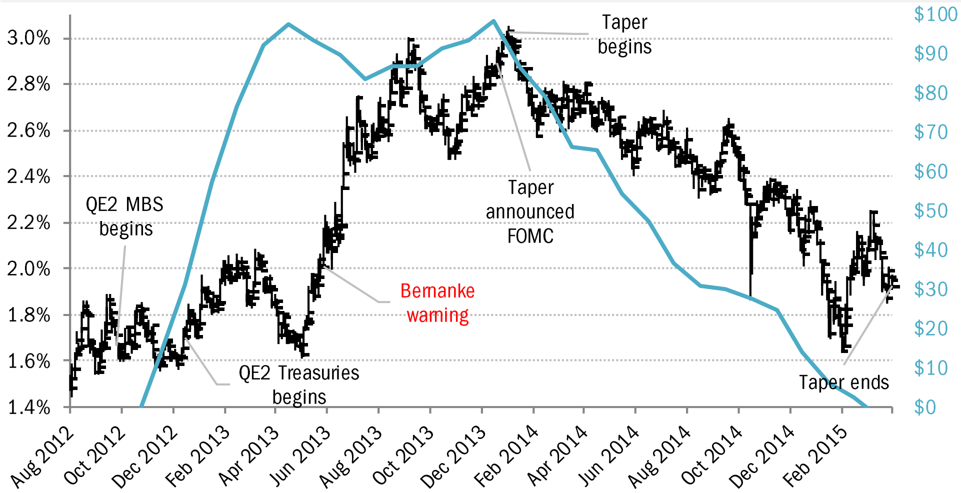
Source: Federal Reserve Board, TrendMacro calculations

minutes of the April meeting (see "Data Insights: FOMC Minutes" May 19, 2021), the Committee has had that talk about talk *already* (see "Video: What you're not hearing about the Fed gearing up to taper" May 20, 2021).

- There was nothing about that in today's FOMC statement nor in the prepared remarks in the post-meeting press conference. In the question-and-answer session, Powell rather elegantly sidelined the matter saying that "this was the talking about talking about meeting," so "now it's time to retire the term" (remember, he falsely stated in the April presser that no such conversations were taking place, but the minutes revealed that they were). His go-to talking point now is just to retreat to a version of the statement language, that asset purchases will continue "until substantial further progress has been made toward the Committee's maximum employment and price stability goals."
- As of this writing, the 10-year yield is notably higher. It's not clear to us that this is the result of some sense that tapering will come sooner than previously expected, or the result of taking on board the SEP's cue that growth needs to be upgraded.
- We caution against worrying to much about a "taper tantrum." The 2013 "temper tantrum" – of which any clients fear a replay – is mostly a false memory (see "Video: Three things you aren't hearing

[about the coming taper tantrum”](#) June 7, 2021). To be sure, the 10-year yield backed up as almost 100 bp over seven months from when [then-chair Ben Bernanke first dropped the hint in late May](#) (please see the chart below). *Yields fell the moment actual tapering began seven months later, and kept falling, to the point where they were lower by the time tapering was complete than they had been when Bernanke first brought up the subject*.

“Taper tantrum” — US 10-yr Treasury yield (nominal) — Fed LSAPs (per month, USD billions)



Source: Bloomberg, TrendMacro calculations

- *We think that yields should move higher almost no matter what the Fed says about purchases, considering how weirdly low they are amidst an increasingly obvious economic boom.*

Finally, we had expected Powell to take a lot of flak in the press conference about high inflation rates in the most recent two Consumer Price Index reports (see [“What you're not hearing about today's horrible CPI data”](#) June 10, 2021). In fact, we expected him to repeat the word “transitory” *ad nauseam* (he ended up saying it only once). The subject came up, but wasn’t pushed very hard by Powell’s questioners. We take this, casually, as a sign that the consensus has been persuaded that the present bout of price increases is, in fact, transitory even if Powell doesn’t have to use the word excessively.

- *To be sure, that’s a form of complacency that sets up for a market break if it is proved wrong. Be that as it may, we think it’s the right expectation. And it’s self-fulfilling: Powell’s ability to contribute to a consensus that inflation is well-anchored longer term favorably shapes the expectations-driven behaviors that make it true.*

Bottom line

The 2023 “dots” now forecast two rate hikes, up from zero forecasted in May. But this only matches expectations already embedded in forward prices. The

SEP upgraded expectations for growth, unemployment and inflation. It's something of an embarrassment that the forecasted real GDP growth rate for 2023, without assuming the White House's massive spending proposals, is higher than the White House's own forecast that does assume them – implying the economy is better off with them. Moreover, Powell admitted that unemployed persons will seek work when enhanced unemployment benefits run off, suggesting that the benefits were a policy error. Neither help Powell's re-appointment prospects. Powell finessed the question of tapering, moving past the "talking about talking about" trope. Yields should move higher regardless in virtue of improving growth. Inflation was not intensely questioned in the presser, anecdotal evidence that self-fulfilling expectations are anchored.