

FED SHADOW

**“Hawkish Powell”? Not a Chance.**

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**It’s performative politicking ahead of confirmation by an inflation-obsessed Senate.**

The Fed-watching community is getting way ahead of itself with headlines like this one [on Bloomberg](#): “Hawkish Powell Is a Force Markets Haven’t Faced in Three Years” – or this one [on Fox News](#): “Powell admits Fed got it wrong on inflation, says they should stop calling it ‘transitory.’”

- *Fed Chair Jerome Powell is a politician who, having earned renomination (as we predicted: see [“Powell or Brainard? Or...?”](#) November 17, 2021), now faces Senate confirmation hearings conducted by other politicians, all of whom, Republicans and Democrats alike, find it useful to pretend to be obsessed with inflation.*
- For example, in the fight for the Build Back Better Act, [Republicans say it will fuel inflation](#) and [Democrats say it will solve it](#) – but both parties agree that inflation is center-stage with voters.
- *So Powell, too, has to pretend to be obsessed with inflation. Once he is confirmed in January he’ll snap right back to his obsession with “inclusive maximum employment” (see [“Video: What you’re not hearing about the Fed’s liftoff from zero policy rates”](#) October 26, 2021).*
- *Powell’s statement to Senate Banking Committee Ranking Member Patrick Toomey (R-PA), in questions following testimony, that “it’s probably a good time to retire that that word” – that is, “transitory” as a description of the present elevated inflation statistics – has been taken woefully out of context. Powell is by no means saying he believes inflation is not transitory.*
- For goodness sake – *he said outright in his prepared testimony that “Most forecasters, including at the Fed, continue to expect that inflation will move down significantly over the next year as supply and demand imbalances abate.”*
- Rather, Powell was responding to Toomey’s mocking questioning – “...everything’s transitory; life is transitory. How long does inflation have to run above your target before the Fed decides maybe it’s not so transitory?”
- Powell replied by bemoaning the fact that “the word transitory has different meanings to different people.” But the full sentence containing the word “retire” was: “I think it’s probably a good time to retire that word and try to explain more clearly what we mean.”

**Update to strategic view**

**FEDERAL RESERVE, US MACRO:** Powell “retiring” the word “transitory” to describe inflation by no means implies he thinks it’s not actually transitory. It was performative politics in which Powell, facing Senate confirmation, had to cater to Senators’ obsession with inflation. Retiring the word was a response to a silly question revealing its ambiguity, giving Powell a chance to clear up misunderstandings. He clarified it means inflation won’t “leave a mark,” which we understand to mean won’t perturb long-term inflation expectations, which remain entirely quiescent. Accelerating the tapering of asset purchases is a free option for Powell. It gives him a way to be seen as doing something about inflation, but acceleration will have no economic consequences whatsoever. He can use it to avoid the destructive consequences of having to bring lift-off from near-zero policy rates forward in time before the goal of inclusive maximum employment is met.

[\[Strategy dashboard\]](#)

- He explained, “We tend to use it to mean that it won’t leave a permanent mark in the form of higher inflation.” Not the most articulate explanation, but it surely means that “transitory” refers to a regression of the rate-of-change of prices back to target, not a deflationary reversal of the price level itself. In other words, the present inflation will represent a step-function higher in prices, after which, in due time, the rate of change will be at-target. In conversations with clients we ourselves constantly encounter that ambiguity, and it is useful to have Powell clarify it (see [“Is Inflation Still ‘Transitory’?”](#) October 13, 2021).
- What would it mean to “leave a mark”? It seems obvious to us that such a “mark” would be an elevation of inflation expectations – which very much has not happened: they are only back to the somewhat below-target levels where they were before the pandemic, after an episode of deflation-fear during the 2020 lockdowns.
- The FOMC’s often-repeated criterion for lift-off from near-zero policy rates – reiterated once again in the [November FOMC statement](#) – is to have “longer-term inflation expectations remain well anchored at 2 percent,” and that has not happened. For example, five-year five-years-forward TIPS breakevens aren’t there, when downward-adjusted 50 bp to put the Consumer Price Index on which they are based on historical par with the Personal Consumption Expenditures Price Index that the Fed uses as its target (please see the chart below – and by the way, that downward adjustment is more than fair, with PCE inflation having run a full percentage point lower than CPI this year).

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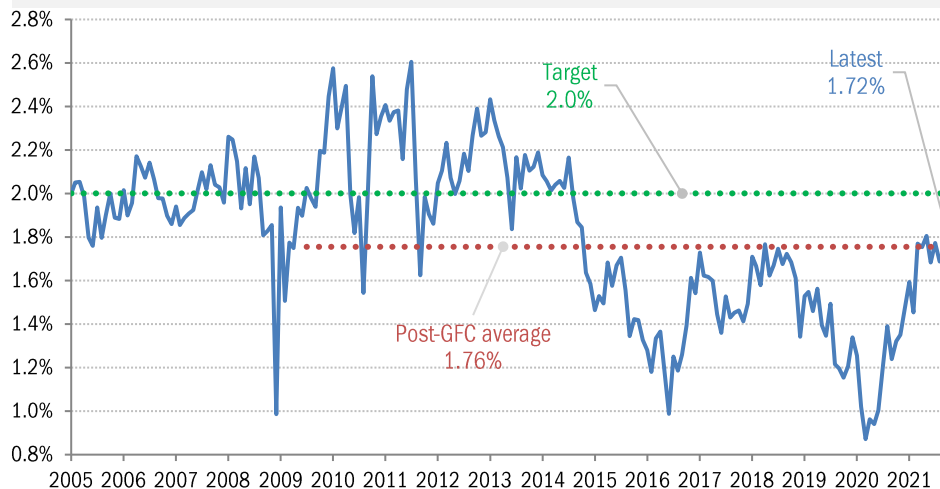
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Five-year five-years forward TIPS breakeven (downward adjusted 50 bp for PCE basis)



Source: Bloomberg, TrendMacro calculations

- What about Powell’s statement that “it is...appropriate, in my view, to consider wrapping up the taper of our asset purchases, which we actually announced at the November meeting, perhaps a few months sooner”?
- This is more than a casual remark in the context of answering a silly question – this is a hint of a policy change. But it’s a brilliant

move, because the pace of tapering, we believe, whether it is accelerated, decelerated or anything else, makes no difference whatsoever to economic outcomes at this point – yet fine-tuning it gives Powell the opportunity to be seen as “doing something about inflation.” Asset purchases are emergency measures when the economy needs the Fed to be the risk-taker of last resort, and the economy plainly has no such need now (see, among many, [“Video What you aren't hearing about the Fed's taper talk”](#) August 19, 2021). So accelerating the taper now is a free political option for Powell, which he can exercise as part of the performative politics of confirmation, while holding his fire on potentially destructive “lift-off”.

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### Bottom line

Powell “retiring” the word “transitory” to describe inflation by no means implies he thinks it’s not actually transitory. It was performative politics in which Powell, facing Senate confirmation, had to cater to Senators’ obsession with inflation. Retiring the word was a response to a silly question revealing its ambiguity, giving Powell a chance to clear up misunderstandings. He clarified it means inflation won’t “leave a mark,” which we understand to mean won’t perturb long-term inflation expectations, which remain entirely quiescent. Accelerating the tapering of asset purchases is a free option for Powell. It gives him a way to be seen as doing something about inflation, but acceleration will have no economic consequences whatsoever. He can use it to avoid the destructive consequences of having to bring lift-off from near-zero policy rates forward in time before the goal of inclusive maximum employment is met. ▶