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TRENDMACRO LIVE!

On the December FOMC

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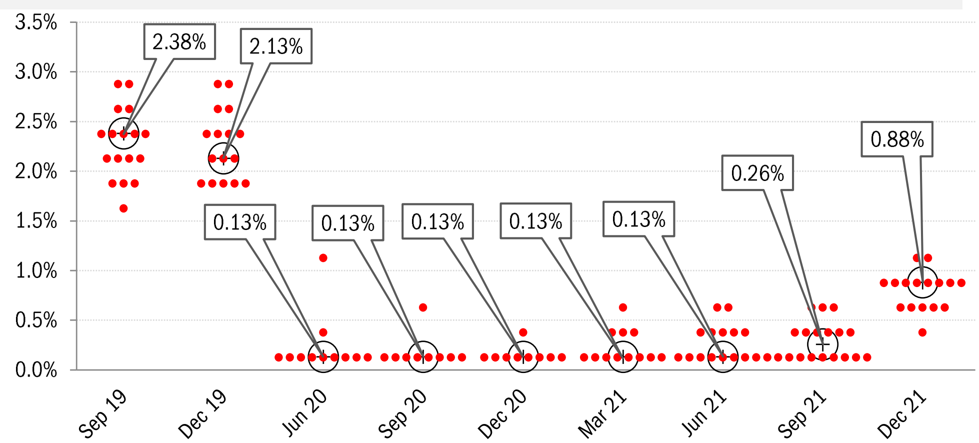
The word "transitory" was dutifully retired. But the FOMC still says inflation is transitory.

Today's FOMC statement expertly navigated the dire political challenges we outlined yesterday, which might have made this the most consequential FOMC meeting in years (see "Jay Powell: Inflation Justice Warrior" December 14, 2021).

- As expected, the pace of tapering asset purchases has been doubled, implying it will be complete by March. Once again, *we believe that QE has long ago stopped serving any economic function, so the rate at which it is ended has no market consequences – except that it can be used by the Fed to claim it is "doing something" about inflation (without really doing anything: it won't reduce inflation, but it won't harm the economy either).*
- Of course, with respect to inflation, the word "transitory" was expunged, or rather "retired," as Chair Jerome Powell said it should be in Senate testimony two week ago (see "'Hawkish Powell'? Not a Chance." December 1, 2021). *However, the statement said, "Supply and demand imbalances related to the pandemic and the reopening of the economy have continued to contribute to elevated levels of inflation." That is to say, inflation is transitory, because those imbalances are transitory.*
- *And that is also to say that inflation has real-economy origins, not monetary policy origins, which would suggest that it's a real-*

Estimated appropriate 2022 funds rate in SEP, by FOMC meeting



Source: Federal Reserve Board, TrendMacro calculations

Update to strategic view

FEDERAL RESERVE, US MACRO: Powell successfully navigated dire political challenges. The FOMC doubled the pace of tapering of asset purchases, pointing to a March wind-up, to address concerns that the Fed is "doing something" about high inflation. It won't reduce inflation, but it won't harm the economy. The SEP upgraded the number of 2022 rate hikes from one half to three, in line with market expectations. The word "transitory" was dropped from the FOMC statement, but attributing it to supply-demand mismatches means it is still regarded as transitory nevertheless. In the presser, Powell said he doesn't believe wage growth is contributing to inflation – another argument for transitory. The SEP estimate for 2022 inflation was raised to 2.7% from 2.3% – but compared to present levels, very much transitory. The key takeaway is that Powell did not utter so much as a single syllable suggesting that his Fed will try to slow the economy to fight an inflation wrongly believed to not be transitory.

[Strategy dashboard]

economy solution that's required, not a policy solution – that is, not an aggressive or accelerated hiking cycle.

- *Also, in the post-meeting press conference, he noted that "wage growth has not been a significant contributor" to above-target inflation. Again, that is to say it is still transitory.*
- The inflation estimates in the Summary of Economic Projections underscores the Fed continues to see inflation as transitory, whatever words they may use to say so. The estimate for Personal Consumption Expenditures inflation this year has been upgraded to 5.3% from 4.2% – but that's not saying much with just one month to go. *For next year, the upgrade for PCE inflation is from 2.2% to 2.6% – above target, to be sure, but basically still transitory* (see "Data Insights: Federal Reserve" December 15, 2021).
- The SEP upgraded participants' estimates of the appropriate policy rate for 2022 to 0.88% from 0.26% – that is, *to three rate hikes from half a rate hike*, broadly in line with the market's recent bringing-forward of lift-off to June from September (please see the chart on the first page and, again, see "Jay Powell: Inflation Justice Warrior").
- The statement effectively declared the inflation component of the criteria for lift-off to have been already met. The maximum employment component remains unmet.
- In the post-meeting press conference, Powell noted that the November jobs report showed that the economy had "narrowed the differences in unemployment among groups." As we have pointed out, the Powell Fed insists that maximum employment be "inclusive" – and what he's saying here is that it is moving toward just that.
- He went on to note that the restoration of the labor force to pre-pandemic levels still has considerable ground to cover. Of all the dimensions of "maximum employment," this is the one most likely at this point to emerge as a reason to defer lift-off.
- *Powell nailed it. The key takeaway is that he didn't utter a single syllable suggesting the Fed will get maneuvered by political pressures into slowing the economy for the sake of reducing inflation that is, in fact, transitory – and that Fed policy didn't create in the first place.*

Bottom line

Powell successfully navigated dire political challenges. The FOMC doubled the pace of tapering of asset purchases, pointing to a March wind-up, to address concerns that the Fed is "doing something" about high inflation. It won't reduce inflation, but it won't harm the economy. The SEP upgraded the number of 2022 rate hikes from one half to three, in line with market expectations. The word "transitory" was dropped from the FOMC statement, but attributing it to supply-demand mismatches means it is still regarded as transitory nevertheless. In the presser, Powell said he doesn't believe wage growth is contributing to inflation – another argument for transitory. The SEP estimate for 2022 inflation was raised to 2.7% from 2.3% – but compared to present levels, very much transitory. The key takeaway is that Powell did not utter so much as a single syllable suggesting that his Fed will try to slow the economy to fight an inflation wrongly believed to not be transitory.