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TRENDMACRO LIVE!

On the March FOMC: Dots in the Headlights

Wednesday, March 19, 2025

Donald Luskin

The Powell Put is in place – and with the end of QT, it's already being deployed.

We were wrong when we said the FOMC would lower its "dot plot" for year-end 2025 (see "Uncertainty Has Become a Cliché" March 17, 2025). By the time the Summary of Economic Projections was released, markets had already moved give very little probability to a move in the dots, so that's not a surprise. But as of this writing, *despite no move in the dots, expectations have moved lower than they were pre-meeting. Why?*

This FOMC is all about uncertainty, with the only language change in today's FOMC statement to say that it "has increased." The SEP lowered the growth estimate for 2025, and raised unemployment estimate (see "Data Insights: Federal Reserve" March 19, 2025). Inflation estimates were raised – so *the Fed finds itself a deer in the headlights, caught between its two mandates, unable to move. At least in rate policy. But the surprise at*

Update to strategic view

FEDERAL RESERVE, US MACRO: The SEP lowered growth estimates, and raised unemployment estimates. Yet the "dot plots" didn't move, leaving expected rate policy frozen. Inflation estimates were raised, and we learned in the presser …

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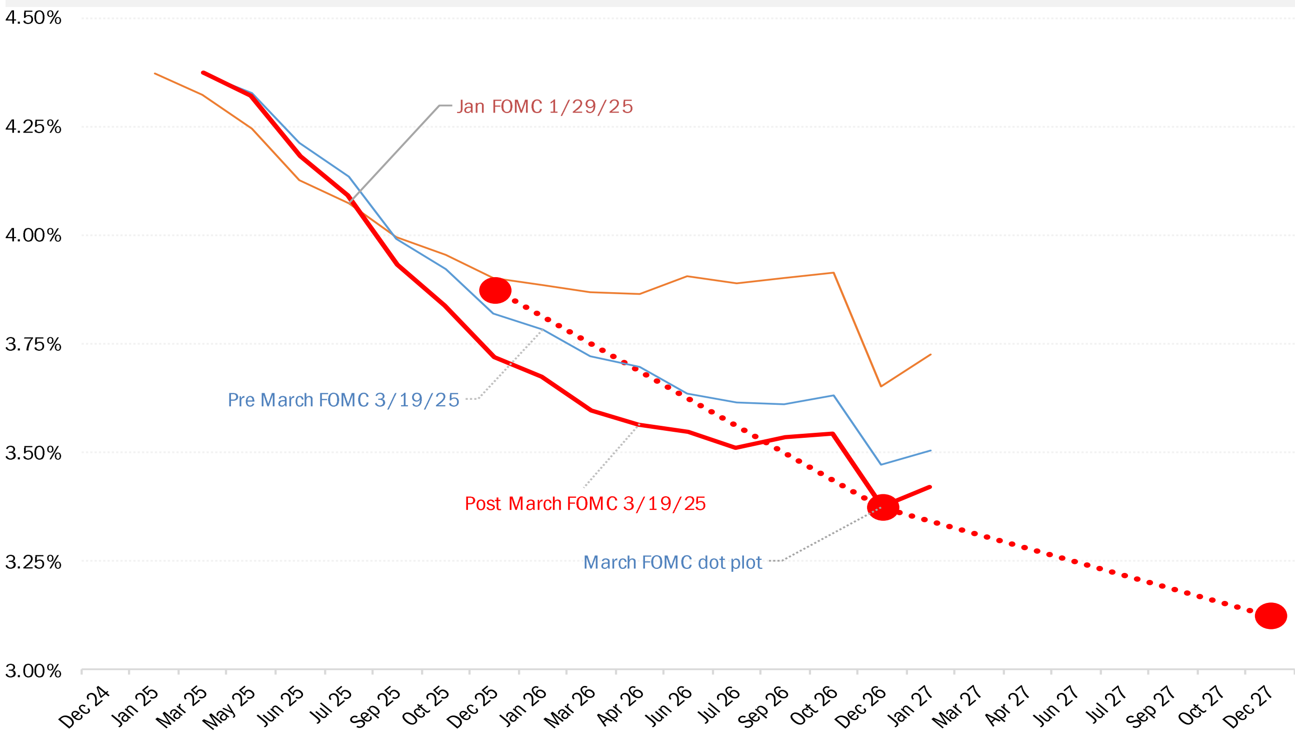
Futures-implied effective funds rate versus "dot plots" of "appropriate policy path" (adjusted to target midpoint)



Source: FRB SEP, TrendMacro calculations *this FOMC was the announcement of what amounts to an end to "quantitative tightening," with the monthly redemption cap on maturing Treasuries on the Fed's balance sheet reduced from $25 billion to only $5 billion.* In the prepared remarks before the post-meeting press conference, *Powell explained the move as the result of observing some degree of "tightness" in "money markets."*

This FOMC has come down squarely on the dove side, and the futures curve is seeing it. The Powell Put is there, and has begun to be deployed.

- Influential Governor Christopher Waller found himself the odd man out this time, issuing a dissent against reducing the redemption cap.
- Kevin Hassett, Director of National Economic Council, said earlier today the Fed is on "cruise control." Luckily Powell didn't say that today, or it would substantially repeat his famous gaffe at the December 2018 FOMC when he said the quantitative tightening was "on automatic pilot." With the emphasis on uncertainty and the virtual end of QT, *this FOMC is very much not on automatic pilot.*

The first question in the presser was whether the SEP upgrade of its 2025 inflation estimate versus December was due to tariffs. Powell stammered out some platitudes about how difficult it is to attribute causes to inflation or anything else – but *never said whether or not the estimates were raised because of tariffs. That means they probably were*.

- *Indeed, more than 30 minutes into the presser, another reporter asked the same question and this time Powell decided to be honest about it: "without exception" the contributors to the "dot plots" built tariff assumptions into their higher inflation estimates.*
- To yet another question near the end, he amplified that these assumptions included expected retaliation. *Clearly, the committee's economic forecasting has gotten way over its skis – no one has any idea how our incipient trade war is going to play out.*
- Rate policy, then, is hostage (1) to the degree to which tariffs are actually implemented (as opposed to just threatened); (2) to the degree that any actual tariffs do feed into inflation; and (3) whether some future FOMC decides it is appropriate to adjust rates for that reason.
- It's hard to know what Powell and his colleagues really know or believe about this. In response to a snarky question about his failure to deal promptly with "transitory" inflation in 2021, Powell quipped that tariff-driven inflation was indeed transitory in the 2018-2019 episode – as though he'd been reading our work on that (see "How Much Do Tariffs Matter?" January 28, 2025);
- But he can't seem to hold onto subtleties for long. *Powell said later in the presser, as though it were an axiom requiring no proof, that "tariffs tend to bring inflation up and growth down." So what's a dual-mandate central bank to do? Deer in the headlights*.

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… it was due to every participant making very specific and elaborate assumptions about the inflationary and anti-growth effects of US tariffs and global retaliation, despite Powell's repeated claims, indeed language in the statement, that "uncertainty...has increased." Apparently unable to agree on any adjustment to rate policy in light of threats to both sides of the Fed's mandate, the monthly redemption cap on Treasuries was cut by 80%, virtually ending quantitative tightening – despite a dissent on that from Waller. The Powell Put is in place, and it is beginning to be deployed.

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AI podcast version

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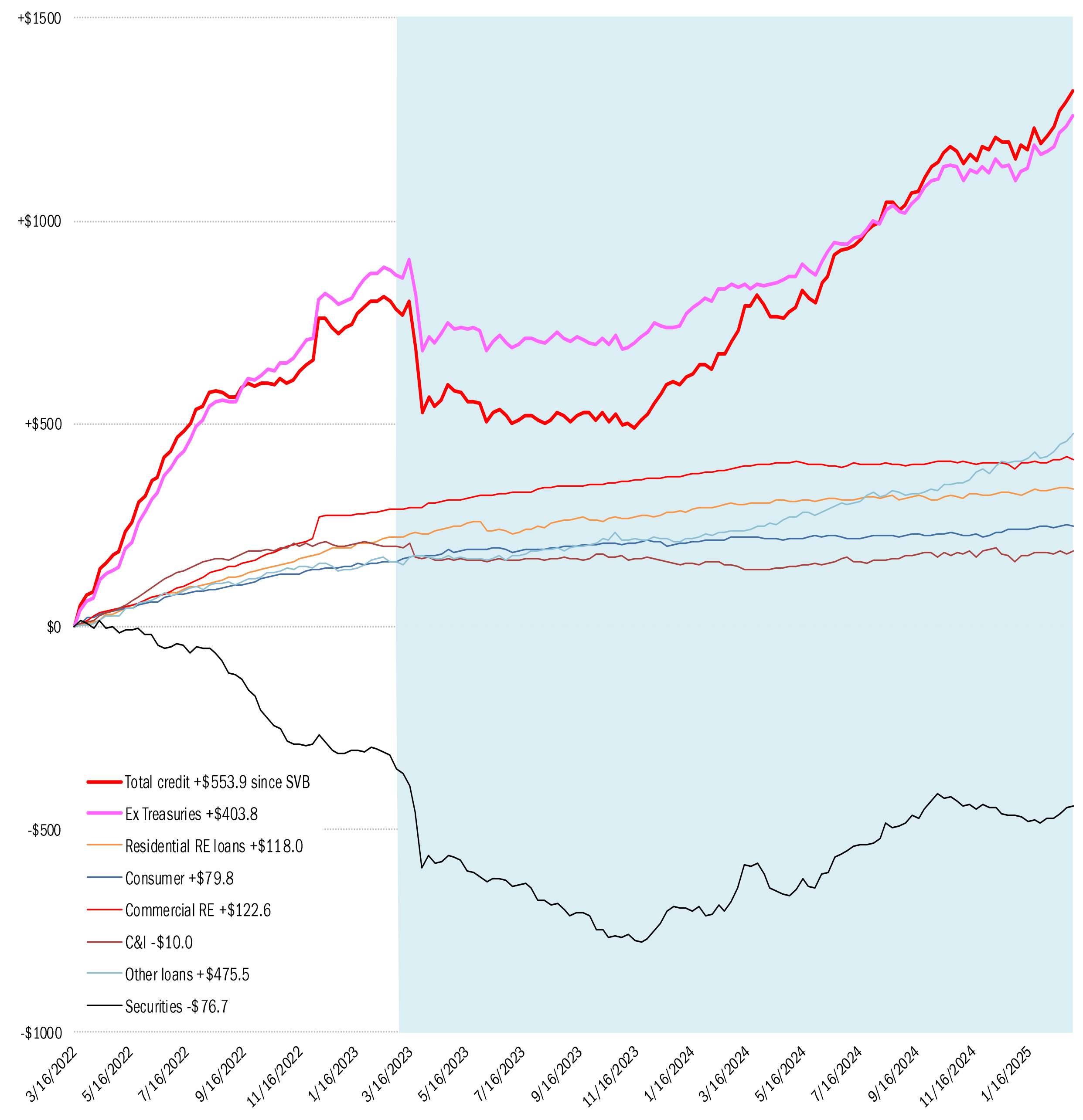
Remember – AI can be funky. This is still experimental. Check it out and let us know what you think.

In other Fed news, Trump has nominated sitting Governor Michelle Bowman to be the statutory Vice Chair for Supervision, a position that enjoys more power over the Fed's regulatory mission than Powell's position of Chair. She is a former Kansas banking regulator, appointed to the Board by Trump in 2018. She will be a strong voice for Trump's deregulatory agenda, calling for (in her own words) "transparent and tailored bank regulatory framework that encourages innovation." In other words, lighter and less arbitrary regulation. *Elizabeth Warren: you're fired*..

US-chartered domestic banks, updated weekly from March 2022 lift-off ■ Post-SVB failure

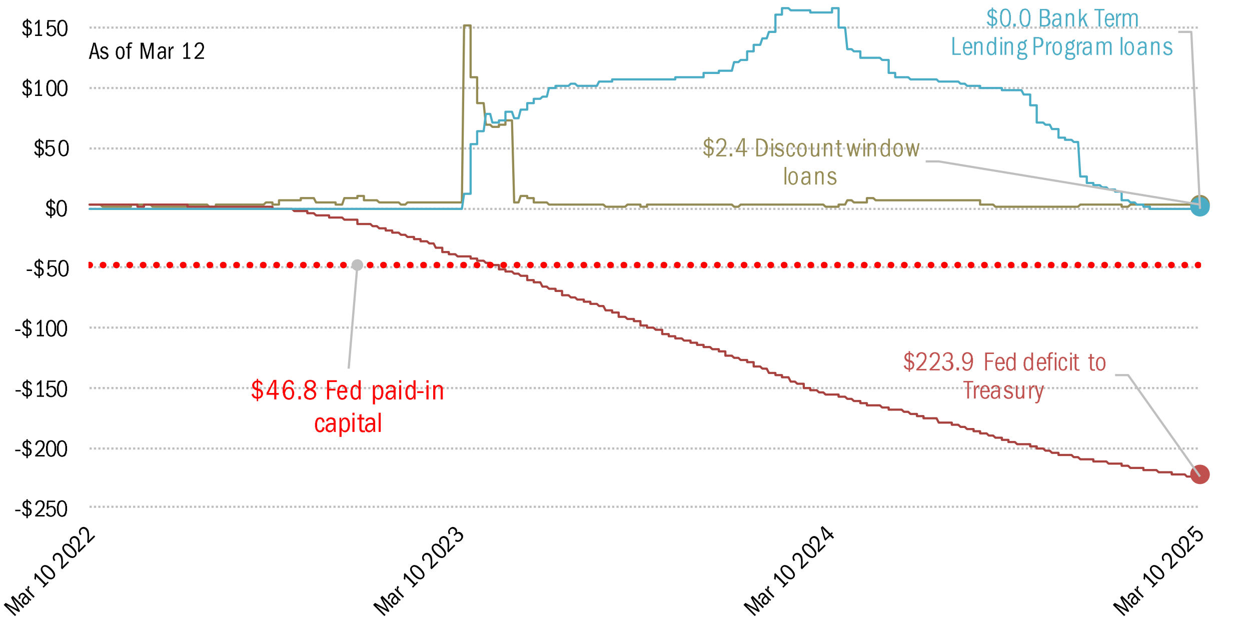


Source: FRB H.8, TrendMacro calculations

We also note that this is the first FOMC after the closure, just last week, of the Bank Term Funding Program, put in place right after the Silicon Valley Bank failure almost two years ago. The program was designed to allow banks with underwater long-term Treasury securities to pledge them to the Fed and receive cash at their par value, rather than their depreciated market value. We said at the time that the program, if it had been in place a week earlier, would have saved SVB (see "It's Over For SVB – And the Fed" March 13, 2023). And we said it would prevent the SVB failure from becoming a systemic "Lehman moment." That was totally correct.

- The BTFP has gracefully wound down, from over $160 billion a year ago (please see the chart below). There has been no significant rise in Discount Window lending to compensate, and loans and leases in bank credit are at all-time highs (please see the chart on the previous page), so *it would appear the crisis has passed, and BTFP succeeded in it's mission, as we expected it would*.
- Well, except that Powell says he sees "tightness" in "money markets." We'll see.
- And it must be said that *the Federal Reserve System itself continues to hold underwater Treasury securities and suffer from negative net interest margins*, the accumulated loss from which is now almost $220 billion (again, please see the chart below). If the Fed were a bank that the Fed regulated, it would be in receivership (see "The Fed is Silicon Valley Bank" April 17, 2023).

Bank relief and cumulative Fed losses on Federal Reserve balance sheet (USD billions)



Source: FRB, TrendMacro calculations

Bottom line

The SEP lowered growth estimates, and raised unemployment estimates. Yet the "dot plots" didn't move, leaving expected rate policy frozen. Inflation estimates were raised, and we learned in the presser it was due to every participant making very specific and elaborate assumptions about the inflationary and anti-growth effects of US tariffs and global retaliation, despite Powell's repeated claims, indeed language in the statement, that "uncertainty...has increased." Apparently unable to agree on any adjustment to rate policy in light of threats to both sides of the Fed's mandate, the monthly redemption cap on Treasuries was cut by 80%, virtually ending quantitative tightening – despite a dissent on that from Waller. The Powell Put is in place, and it is beginning to be deployed.