

FOMC Minutes Intensify References To Dollar Strength

- While the minutes to the September 25th–26th FOMC meeting ([here](#)) didn't contain anything that is directly impactful to markets—indeed, the dollar and Treasuries shook them off—they did contain a number of points worth flagging. **The minutes contained stronger references to dollar concerns and a different explanation of why they deleted 'accommodative' than I had anticipated. There was nothing new on risks to rate guidance that has been provided to date. Of similar interest is what the minutes did not touch upon but might have either now or in the next couple of meetings.**
- **Why did the FOMC decide to remove reference to “accommodative” from the statement?** Their reasoning isn't quite what I had expected. Basically what follows from the quotes is that they did it because they don't really know where neutral lies so they felt they may as well remove the reference now given the number of hikes they have pushed through to date compared to earlier stages when it was more evident that policy was stimulative. They didn't say—and I thought they might have—that they were anchoring the discussion in terms of where the real policy rate currently sits relative to where the real neutral rate sits at this point in the cycle. I'm a bit disappointed they didn't do so as the explanation leans more to how they don't really have a clue about what the longer run guide post for rates may be and whether it may be higher than their 3% estimate or lower. Yet they are comfortable guiding another 125bps of hikes between now and 2020 without really much confidence in their neutral rate estimate.

"With regard to the postmeeting statement, members agreed to remove the sentence indicating that “the stance of monetary policy remains accommodative.” Members made various points regarding the removal of the sentence from the statement. These points included that the characterization of the stance of policy as “accommodative” had provided useful forward guidance in the early stages of the policy normalization process, that this characterization was no longer providing meaningful information in light of uncertainty surrounding the level of the neutral policy rate, that it was appropriate to remove the characterization of the stance from the Committee's statement before the target range for the federal funds rate moved closer to the range of estimates of the neutral policy rate, and that the Committee's earlier communications had helped prepare the public for this change."

"Participants discussed a number of reasons for removing the language at this time, noting that the Committee would not be signaling a change in the expected path for policy, particularly as the target range for the federal funds rate announced after the Committee's meeting would still be below all of the estimates of its longer-run level submitted in the September SEP. In addition, waiting until the target range for the federal funds rate had been increased further to remove the characterization of the policy stance as “accommodative” could convey a false sense of precision in light of the considerable uncertainty surrounding all estimates of the neutral federal funds rate."

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- **Also note that the FOMC specifically flagged dollar strength as a risk in a number of spots within the minutes as follows below.** The tone of the dollar remarks generally escalates some of the concern compared to, say, the June meeting minutes when “a few” flagged dollar strength as a downside risk to the inflation outlook. I think it’s high time they intensified such concerns given Fed estimates that each 10% sustained trade weighted appreciation in the dollar tends to knock core PCE inflation back by ½% within six months and 0.3% within one year. The broad dollar index has been approaching the high points set early in January this year and before that way back during the dot com period. The minutes to the July 31st–August 1st meeting were lighter on dollar references.
 - a) “The divergence between domestic and foreign economic growth prospects and monetary policies was cited as presenting a downside risk because of the potential for further strengthening of the U.S. dollar.”
 - b) “A number of participants noted that financial conditions remained accommodative: The rise in interest rates and appreciation of the dollar over the intermeeting period had been offset by increases in equity prices, and broader measures continued to point to accommodative financial conditions. ”
 - c) “Some participants cited the waning of fiscal stimulus, less accommodative monetary policy, or anticipated appreciation of the dollar as factors contributing to their forecasts for a moderation of real GDP growth over the course of the projection period.”
- **Guidance remained unchanged with respect to raising the nominal policy rate above the long-run estimate of the neutral rate.** Remember that the FOMC consensus had forecast overshooting the neutral rate by 50bps by 2020 and sustaining this into 2021.
- **Neutral rate guidance itself is unchanged** by way of any fringe debates.
- **I would discount their reference to “uncertainty regarding trade policy”** since the meeting preceded the NAFTA 2.0 / USMCA agreement by a few days. That said, they mentioned trade policy uncertainty three times in the participants discussion.
- **At least two topics might have been broached but were not just yet;** that might defer risk of discussion on these matters to the two remaining meetings this year. For one, there was **no discussion of balance sheet management**. Recall that the minutes to the prior meeting said there would be such a discussion of “operating frameworks before too long....in the fall.” Technically the September 23rd meeting fell within the Fall that began on September 22nd but it was a stretch to expect such a discussion this soon. Watch for the November or December meetings. There was also **no discussion of counter cyclical capital buffers**.
- What follows is a collection of FOMC opinions along a variety of topics categorized according to the Fed’s language used to convey the frequency of citation.

All

“Based on recent readings on spending, employment, and inflation, almost all participants saw little change in their assessment of the economic outlook.”

“Based on their current assessments, all participants expressed the view that it would be appropriate for the Committee to continue its gradual approach to policy firming by raising the target range for the federal funds rate 25 basis points at this meeting.”

“All participants anticipated that real GDP growth would moderate in the coming years, and a majority of participants projected growth in 2021 to be below their estimates of the longer-run rate.”

“All participants who submitted longer-run projections expected that the unemployment rate would run below their estimates of its longer-run level throughout the projection period.”

“All participants continued to express the view that the appropriate trajectory of the federal funds rate would likely involve gradual increases.”

Generally Agreed

“For the economy overall, participants generally agreed that, on balance, recent data suggested some acceleration in labor costs, but that wage growth remained moderate by historical standards, which was due in part to tepid productivity growth.”

“Participants generally agreed that risks to the outlook appeared roughly balanced.”

Nearly All

“Nearly all participants viewed the degree of uncertainty attached to their economic projections for real GDP growth and inflation as broadly similar to the average of the past 20 years.”

Almost all

“Based on recent readings on spending, employment, and inflation, almost all participants saw little change in their assessment of the economic outlook.”

“Almost all considered that it was also appropriate to revise the Committee’s postmeeting statement in order to remove the language stating that “the stance of monetary policy remains accommodative.”

“Almost all participants continued to expect that the evolution of the economy, relative to their objectives of maximum employment and 2 percent inflation, would likely warrant further gradual increases in the federal funds rate.”

“Almost all participants continued to express the view that the appropriate trajectory of the federal funds rate would likely involve gradual increases.”

All but one

- none

Majority

“A majority of participants projected growth in 2021 to be below their estimates of the longer-run rate.”

“A solid majority of participants marked up their projections of real GDP growth and most increased their forecast of the unemployment rate in 2018, with 1 Four members of the Board of Governors, one more than in June 2018, were in office at the time of the September 2018 meeting and submitted economic projections. The office of the president of the Federal Reserve Bank of San Francisco participants indicating that these revisions mostly reflected incoming data.”

“A substantial majority of participants expected that the year-end 2020 and 2021 federal funds rate would be above their estimates of the longer-run rate.”

“Participants’ projections for real GDP growth in 2021 were almost all below participants’ projections of growth in 2020 and, for a majority of participants, below their longer-run projections of real GDP growth.”

“A substantial majority of participants expected the unemployment rate to bottom out in 2019 or 2020 at levels below their estimates of the unemployment rate in the longer run, and then to rise a little in 2021.”

“Risks around both total and core inflation projections were judged to be broadly balanced by a solid majority of participants; however, those participants who saw the risks as uneven saw them as weighted to the upside.”

Most

“Most increased their forecast of the unemployment rate in 2018, with participants indicating that these revisions mostly reflected incoming data.”

“While most participants made slight upward revisions to their unemployment rate projections for this year, their projections in subsequent years and in the longer run were largely unchanged.”

“Most participants projected total PCE price inflation in the range of 1.9 to 2.0 percent for 2018 and 2019 and 2.1 to 2.2 percent in 2020 and 2021.”

“Most participants projected that core PCE inflation would run at 1.9 to 2.0 percent in 2018 and at 2.1 to 2.2 percent in 2019, 2020, and 2021.”

“Most participants assessed the risks to their projections of real GDP growth and the unemployment rate as broadly balanced—in other words, as broadly consistent with a symmetric fan chart.”

More than half

- none

Fewer than half

- none

Several

“Several participants noted that the household saving rate had been revised up significantly in the most recent estimates published by the Bureau of Economic Activity. A few of those participants remarked that the upward revision in the saving rate could be viewed as evidence of the strength of the financial position of the household sector and could be a factor that would further support solid expansion of consumption spending.”

“Several participants commented that inflation may modestly exceed 2 percent for a period of time.”

“Several participants reported that firms in their Districts that were facing higher input prices because of tariffs perceived that they had an increased ability to raise the prices of their products.”

“The median projection for the longer run federal funds rate rose slightly, with several participants citing increases in model-based estimates of the longer-run real federal funds rate and strong economic data as reasons for the revision.”

Many

“In discussing the uncertainty and risks surrounding their economic projections, many participants pointed to upside risks to real GDP growth from fiscal stimulus or stronger-than-expected effects of business optimism.”

Some

“Some participants commented about the continued growth in leveraged loans, the loosening of terms and standards on these loans, or the growth of this activity in the nonbank sector as reasons to remain mindful of vulnerabilities and possible risks to financial stability.”

“Some participants commented that trade policy developments remained a source of uncertainty for the outlook for domestic growth and inflation.”

A number

“A number of participants observed that the stimulative effects of the changes in fiscal policy would likely diminish over the next several years.”

“Relative to the June SEP, a number of participants revised slightly down their projections for total PCE inflation this year and next.”

A few

“A few participants expected that policy would need to become modestly restrictive for a time and a number judged that it would be necessary to temporarily raise the federal funds rate above their assessments of its longer-run level in order to reduce the risk of a sustained overshooting of the Committee’s 2 percent inflation objective or the risk posed by significant financial imbalances.”

“A few participants offered perspectives on the term structure of interest rates and what a potential inversion of the yield curve might signal about economic prospects in light of the historical regularity that an inverted yield curve has often preceded the onset of recessions in the United States. On the one hand, an inverted yield curve could indicate an increased risk of recession; on the other hand, the low level of term premiums in recent years—reflecting, in part, central bank asset purchases— could temper the reliability of the slope of the yield curve as an indicator of future economic activity. In addition, the recent rise and possible further increases in longer term interest rates might diminish the likelihood that the yield curve would invert in the near term.”

“Based on recent readings on spending, employment, and inflation, almost all participants saw little change in their assessment of the economic outlook, although a few of them judged that recent data pointed to a pace of economic activity that was stronger than they had expected earlier this year.”

“A few of those participants remarked that the upward revision in the saving rate could be viewed as evidence of the strength of the financial position of the household sector and could be a factor that would further support solid expansion of consumption spending.”

“A few participants noted weak residential construction activity at the national or District level, which was attributed in part to higher interest rates or supply constraints.”

“A few commented that recent changes in federal tax policy had likely bolstered investment spending.”

“A few participants expected that policy would need to become modestly restrictive for a time and a number judged that it would be necessary to temporarily raise the federal funds rate above their assessments of its longer-run level in order to reduce the risk of a sustained overshooting of the Committee’s 2 percent inflation objective or the risk posed by significant financial imbalances.”

A couple

“However, a couple of participants noted that the higher saving rate may not be a precursor to higher future consumption growth. For example, the higher saving rate may indicate some greater caution on the part of consumers, greater inequality of income and wealth—which would imply a lower aggregate propensity to spend—or changing consumer behavior in a low interest rate environment.”

“A couple of participants emphasized that because inflation had run below the Committee’s 2 percent objective for the past several years, some measures of trend inflation or longer-term inflation expectations were below levels consistent with the 2 percent objective; these participants judged that a modest increase in inflation expectations would be important for achieving the inflation objective on a sustained basis.”

“A couple of participants indicated that they would not favor adopting a restrictive policy stance in the absence of clear signs of an overheating economy and rising inflation.”

“Risks to their outlooks were viewed as balanced, although a couple more participants than in June saw risks to their inflation projections as weighted to the upside.”

“A couple more participants than in June viewed the uncertainty around the unemployment rate as higher than average.”

One

- none

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