

FOMC Minutes Lean Against Rate Cut Pricing

- If one was looking for the FOMC minutes ([here](#)) to feed the market's confirmation bias in favour of rate cut guidance, then one would have been disappointed. Ergo, the US 2 year Treasury cheapened a touch in the immediate aftermath and the USD very slightly strengthened.
- **The minutes guide as much against a rate hike this year as they do against a rate cut. Given that markets are pricing toward a rate cut later this year, the message is that the FOMC believes markets are too dovish.** This is backed by two remarks: a central tendency reference to staying on hold this year but not committing to 2020; and a minority opinion that leaves the door open to a hike later in the year. There is no reference to a minority opinion in favour of a cut. Here are the relevant passages:

“Most participants expected that the evolution of the economy, relative to their objectives of maximum employment and 2 percent inflation, would likely warrant keeping the federal funds rate at its current level through the end of 2019.”

“Some participants indicated that if the economy evolved as they currently expected, with economic growth above its longer run trend rate, they would likely judge it appropriate to raise the target range for the federal funds rate modestly later this year.”

- **This message is further backed by the inflation guidance:**

“Almost all participants projected that inflation, as measured by the four-quarter percentage change in the price index for personal consumption expenditures (PCE), would increase slightly over the next two years, and most participants expected that it would be at or slightly above the Committee's 2 percent objective in 2020 and 2021.”

In addition, **one could position the Fed as open minded toward bidirectional risks without skewing them in one direction or the other.** Relative to market pricing for a cut, the message is clear: the Fed isn't skewing its balance of risks in that direction.

“A substantial majority of participants continued to view the degree of uncertainty attached to their economic projections for real GDP growth, unemployment, and inflation as broadly similar to the average of the past 20 years.”

- **Lastly, on the yield curve, the FOMC rightly flags that today's distortions make historical comparisons of limited use as a strong argument against using the curve to forecast recession:**

“Several participants expressed concern that the yield curve for Treasury securities was now quite flat and noted that historical evidence suggested that an inverted yield curve could portend economic weakness; however, their discussion also noted that the unusually low level of term premiums in longer-term interest rates made historical relationships a less reliable basis for assessing the implications of the recent behavior of the yield curve.”

- **Notably absent was any further discussion of lingering balance sheet management issues,** although the following quote indicates they will return to matters possibly including altering the duration of SOMA holdings of Treasuries in future meetings:

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"Many participants offered preliminary views on advantages and disadvantages of alternative compositions for the SOMA portfolio. Participants expected to further discuss the longer-run composition of the portfolio at upcoming meetings. "

- Please see below for the fuller spectrum of opinions captured by the minutes using the Fed's frequency of citation language.

All

"All participants agreed that it was appropriate to issue the proposed statement."

"All participants who submitted longer-run projections continued to expect that the unemployment rate would run at or below their estimates of its longer-run level through 2021."

"All participants marked down somewhat their projections for real GDP growth in 2019, and most revised down slightly their projections for total inflation in 2019."

'Generally Agreed' or 'In General'

"In light of these uncertainties as well as continued evidence of muted inflation pressures, participants generally agreed that a patient approach to determining future adjustments to the target range for the federal funds rate remained appropriate."

Nearly All

- None

Almost all

"Most participants continued to expect real GDP growth to edge down over the projection horizon, with almost all participants projecting growth in 2021 to be at or below their estimates of its longer-run rate."

"Almost all participants projected that inflation, as measured by the four-quarter percentage change in the price index for personal consumption expenditures (PCE), would increase slightly over the next two years, and most participants expected that it would be at or slightly above the Committee's 2 percent objective in 2020 and 2021."

"Almost all participants expected that total and core PCE price inflation would be between 1.8 and 2.2 percent throughout the projection horizon."

All but one

- none

Majority

"With regard to the outlook for monetary policy beyond this meeting, a majority of participants expected that the evolution of the economic outlook and risks to the outlook would likely warrant leaving the target range unchanged for the remainder of the year."

"A substantial majority of participants continued to view the degree of uncertainty attached to their economic projections for real GDP growth, unemployment, and inflation as broadly similar to the average of the past 20 years."

Most

- "Most participants continued to expect real GDP growth to edge down over the projection horizon, with almost all participants projecting growth in 2021 to be at or below their estimates of its longer-run rate."

“Almost all participants projected that inflation, as measured by the four-quarter percentage change in the price index for personal consumption expenditures (PCE), would increase slightly over the next two years, and most participants expected that it would be at or slightly above the Committee’s 2 percent objective in 2020 and 2021.”

“Most participants expected that the evolution of the economy, relative to their objectives of maximum employment and 2 percent inflation, would likely warrant keeping the federal funds rate at its current level through the end of 2019.”

“Most participants mentioned a recent patch of weaker data on domestic economic activity, and some pointed to a softer global growth outlook, as factors behind the downward revisions to their near term growth estimates.”

“Nevertheless, most participants continued to project that the unemployment rate in 2021 would be below their estimates of its longer run level.”

Many

“Many participants offered preliminary views on advantages and disadvantages of alternative compositions for the SOMA portfolio. Participants expected to further discuss the longer-run composition of the portfolio at upcoming meetings.”

“Many participants pointed to the weakness in retail sales in December as notable, although they recognized that the data for January had shown a partial recovery in retail sales. Participants also observed that much of the recent softness likely reflected temporary factors, such as the partial federal government shutdown and December’s volatility in financial markets, and that consumer sentiment had recovered after these factors had receded.”

“Consequently, many participants expected consumer spending to proceed at a stronger pace in coming months, supported by favorable underlying factors, including a strong labor market, solid growth in household incomes, improvements in financial conditions and in households’ balance sheet positions, and upbeat consumer sentiment. Participants noted, however, that the continued softness in the housing sector was a concern.”

“However, many participants pointed to signs that the weakness in investment would likely abate.”

“Many participants indicated that, while inflation had been close to 2 percent last year, it was noteworthy that it had not shown greater signs of firming in response to strong labor market conditions and rising nominal wage growth, as well as to the short-term upward pressure on prices arising from tariff increases.”

More than half

- none

Fewer than half

- none

Several

“Several participants suggested that longer term inflation expectations could be at levels somewhat below those consistent with the Committee’s 2 percent inflation objective and that this might make it more difficult to achieve that objective on a sustained basis.”

“Several participants expressed concern that the yield curve for Treasury securities was now quite flat and noted that historical evidence suggested that an inverted yield curve could portend economic weakness; however, their discussion also noted that the unusually low level of term premiums in longer-term interest rates made historical relationships a less reliable basis for assessing the implications of the recent behavior of the yield curve.”

“Several participants pointed to the increased debt issuance and higher leverage of nonfinancial corporations as a development that warranted continued monitoring.”

“Several participants observed that the characterization of the Committee’s approach to monetary policy as “patient” would need to be reviewed regularly as the economic outlook and uncertainties surrounding the outlook evolve.”

“Several of these participants noted that the current target range for the federal funds rate was close to their estimates of its longer-run neutral level and foresaw economic growth continuing near its longer-run trend rate over the forecast period.”

“Several participants noted that their views of the appropriate target range for the federal funds rate could shift in either direction based on incoming data and other developments.”

“Several participants expressed concerns that the public had, at times, misinterpreted the medians of participants’ assessments of the appropriate level for the federal funds rate presented in the SEP as representing the consensus view of the Committee or as suggesting that policy was on a pre-set course.”

“Nonetheless, several participants noted that the policy rate projections in the SEP are a valuable component of the overall information provided about the monetary policy outlook.”

“Several participants observed that limited inflationary pressures during a period of historically low unemployment could be a sign that low inflation expectations were exerting downward pressure on inflation relative to the Committee’s 2 percent inflation target; in addition, subdued inflation pressures could indicate a less tight labor market than suggested by common measures of resource utilization.”

“Consistent with these observations, **several participants noted that various indicators of inflation expectations had remained at the lower end of their historical range**, and a few participants commented that they had recently revised down their estimates of the longer-run unemployment rate consistent with 2 percent inflation.”

A number

“A number of participants judged that economic growth in the remaining quarters of 2019 and in the subsequent couple of years would likely be a little lower, on balance, than they had previously forecast.”

Some

“Some participants indicated that if the economy evolved as they currently expected, with economic growth above its longer run trend rate, they would likely judge it appropriate to raise the target range for the federal funds rate modestly later this year.”

“In light of these considerations, some participants noted that the appropriate response of the federal funds rate to signs of labor market tightening could be modest provided that signs of inflation pressures continued to be limited.”

“Some participants regarded their judgments that the federal funds rate was likely to remain on a very flat trajectory as reflecting other factors, such as low estimates of the longer-run neutral real interest rate or risk management considerations.”

A few

“A few participants observed that the pickup in productivity growth last year was a welcome development helping to bolster potential output and damp inflationary pressures.”

“Participants observed that, following strong job gains in January, there had been little growth in payrolls in February, although **a few participants pointed out that the February reading had likely been affected by adverse weather conditions.**”

“A few participants cited the combination of muted inflation pressures and expanding employment as a possible indication that some slack remained in the labor market.”

“**A few participants noted that there remained a high level of uncertainty associated with international developments, including ongoing trade talks and Brexit deliberations**, although a couple of participants remarked that the risks of adverse outcomes were somewhat lower than in January.”

“A few participants observed that an economic deterioration in the United States, if it occurred, might be amplified by significant debt service burdens for many firms.”

“Consistent with these observations, several participants noted that various indicators of inflation expectations had remained at the lower end of their historical range, and **a few participants commented that they had recently revised down their estimates of the longer-run unemployment rate consistent with 2 percent inflation.**”

“A few participants observed that the appropriate path for policy, insofar as it implied lower interest rates for longer periods of time, could lead to greater financial stability risks.”

A couple

“Low rates of price increases in sectors of the economy that were not cyclically sensitive were cited by a couple of participants as one reason for the recent easing in inflation.”

“A couple of participants stressed that recent readings on survey measures of inflation expectations were also still at low levels.”

“A couple of participants noted that, over the medium term, some easing in payroll growth was to be expected as economic growth slowed to its longer-run trend rate.”

“A few participants noted that there remained a high level of uncertainty associated with international developments, including ongoing trade talks and Brexit deliberations, **although a couple of participants remarked that the risks of adverse outcomes were somewhat lower than in January.**”

“A couple of participants noted that the “patient” characterization should not be seen as limiting the Committee’s options for making policy adjustments when they are deemed appropriate.”

“However, a couple of these participants noted that such financial stability risks could be addressed through appropriate use of countercyclical macro prudential policy tools or other supervisory or regulatory tools.”

One

none

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