

## FOMC Goes On Summer Vacation

- Fed flags progress toward goals...
- ...but repeats it's not quite there yet to merit tapering...
- ...that continues to be expected later this year
- The overall tone was cautiously optimistic...
- ...with hints of less conviction on transitory inflation in timing and magnitude

This meeting's communications were broadly what one would have expected the FOMC to do given the uncertainties, given it wasn't a forecast meeting per se, given the gap before the next meeting on September 22<sup>nd</sup> with Jackson Hole in between and not to mention a likely bun fight over the debt ceiling over coming weeks. **The FOMC struck the right balance between indicating further progress toward tapering and that a deeper taper dialogue occurred at this meeting, but they reinforced nearer-term focus upon the course of data and events over 'coming meetings.'**

So far, that's consistent with our assumption that taper guidance piles up into the Fall before announcing toward late year. Attention now shifts toward subsequent revelations on the tone of the taper dialogue as various FOMC officials take to the podium on the path to the meeting minutes three weeks from today.

### FEW STATEMENT CHANGES

**There were few statement changes, but they leaned in the direction of cautious optimism and progress toward tapering.** See the statement comparison at the back of this note.

- The description of current conditions in the second paragraph was little changed.
- The main change was in the fourth paragraph. They now reference communication on buying US\$120B per month until 'substantial further progress' toward dual mandate goals has been achieved in the past tense (last December) and update their tracking by noting that "since then, the economy has made progress toward these goals."

Treasury yields spiked a touch higher on that "progress" headline and the dollar rallied, until Chair Powell walked it back a bit in the press conference by noting that "we have not reached substantial further progress and have some ground to cover to get there." That's somewhat of a truism to anyone closely following developments, but I guess it meant something to markets.

### CAUTIOUSLY OPTIMISTIC ON COVID-19

**On the Delta variant, Powell sounded cautiously optimistic.** He noted "What we've seen through successive waves is that the economic implications have tended to be lessening. We'll see if that's the case but it's not an unreasonable expectation. It's plausible that people may pull back from some activities. It might weigh on the return to the labour market. We don't have a strong sense of how that will work but we will be monitoring it closely."

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## INFLATION SHIFT?

If I heard correctly, then **the Fed Chair is sounding less and less strident in terms of his conviction that inflation will magically disappear almost at each successive meeting and after every inflation report.** When asked whether they have met their goals on the price stability side of the dual mandate, Powell deferred to the consensus by saying “that is up to the committee.” Whaa? In the past he tended to dive on that grenade himself. This tone shift likely reflects the greater number of FOMC officials speaking out about inflation risk now versus earlier in the year. Powell did repeat that “we think it will move back down to our objective” but that contrasts to his earlier remarks about inflation all being base effect driven which implied a belief that inflation would crash back down. We’re not hearing quite that same message now.

In fact, when pressed further on inflation and whether it has met the policy goal threshold of moderately exceeding 2% for some time, Powell again deferred to the Committee. He went on to dismiss the question by stating “It really isn’t relevant now because we’re looking at tapering purchases and are a ways away from lift-off which we are not at all near. That’s when we will ask that question.” Ok then, a bit defensive there. That’s a significant narrative shift compared to earlier stridency.

When pressed yet again on inflation, Powell did revert to earlier views that most of the inflation overshoot can be tied to a handful of categories that may be temporarily fed by reopening effects and “We think inflation should move down over time.” For a brief moment it sounded like the Powell of several meetings ago, but he then went on to state “We don’t have much confidence in the size or timing of that.” The latter part is also less aggressive than certainly his earlier dismissals of inflation risk but also more recent ones. Powell then went on to note “I would say in the near term the [ed. inflation] risks are to the upside. I would say the medium-term risks will see it return toward our objective.” **Ok then, so you’ve met your objective? Seems so, just without bluntly stating as much.**

Where I thought it got a bit confusing was in Powell’s remark that full employment was usually necessary to get inflation persistence, yet inflation may be transitory despite his remark that “it shouldn’t take long to get there” meaning toward full employment. If so and his assumption in favour of “strong job creation” over the duration of the year comes to fruition, then given the inflation connection through uncertain Phillips curve connections then why wouldn’t inflation be persistent?

It may also be worth repeating my personal view that Chair Powell might be putting too much weight upon transitory upsides and not enough on potentially transitory downsides to present inflation readings in a more balanced fashion (recall [here](#)). Powell still seems to be taking a one-sided view of transitory and indicated it wouldn’t take long to test this. That too is debatable since transitory shouldn’t be defined as a one or two quarter test versus a full cycle perspective in terms of how policy should view the issue.

## BONDS, EARLY HIKES AND MBS

When probed on whether bond markets are saying the Fed is about to over-tighten, Powell said “I don’t think there is a real consensus on what explains the move between meetings. I don’t see in any of that that there is really anything that challenges the credibility of our framework.”

Powell dismissed the prospect of raising the policy rate while still buying assets which largely dismisses the minority view in favour of early rate hikes given the amount of time it is likely to take to wind down net purchases to zero.

Powell also again downplayed the prospect of tapering MBS purchases faster or more aggressively than Treasury purchases by saying there is “little support” on the FOMC for doing so.

**RELEASE DATE: JULY 28, 2021**

The Federal Reserve is committed to using its full range of tools to support the U.S. economy in this challenging time, thereby promoting its maximum employment and price stability goals.

**With progress on vaccinations and strong policy support, indicators of economic activity and employment have continued to strengthen.** The sectors most adversely affected by the pandemic have shown improvement but have not fully recovered. Inflation has risen, largely reflecting transitory factors. Overall financial conditions remain accommodative, in part reflecting policy measures to support the economy and the flow of credit to U.S. households and businesses.

The path of the economy continues to depend on the course of the virus. Progress on vaccinations will likely continue to reduce the effects of the public health crisis on the economy, but risks to the economic outlook remain.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With inflation having run persistently below this longer-run goal, the Committee will aim to achieve inflation moderately above 2 percent for some time so that inflation averages 2 percent over time and longer-term inflation expectations remain well anchored at 2 percent. The Committee expects to maintain an accommodative stance of monetary policy until these outcomes are achieved. The Committee decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time. **Last December**, the Committee indicated that it would continue to increase its holdings of Treasury securities by at least \$80 billion per month and of agency mortgage-backed securities by at least \$40 billion per month until substantial further progress has been made toward its maximum employment and price stability goals. **Since then, the economy has made progress toward these goals**, and the Committee will continue to assess progress in coming meetings. These asset purchases help foster smooth market functioning and accommodative financial conditions, thereby supporting the flow of credit to households and businesses.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

Voting for the monetary policy action were Jerome H. Powell, Chair; John C. Williams, Vice Chair; Thomas I. Barkin; Raphael W. Bostic; Michelle W. Bowman; Lael Brainard; Richard H. Clarida; Mary C. Daly; Charles L. Evans; Randal K. Quarles; and Christopher J. Waller.

**RELEASE DATE: JUNE 16, 2021**

The Federal Reserve is committed to using its full range of tools to support the U.S. economy in this challenging time, thereby promoting its maximum employment and price stability goals.

**Progress on vaccinations has reduced the spread of COVID-19 in the United States. Amid this progress and strong policy support, indicators of economic activity and employment have strengthened.** The sectors most adversely affected by the pandemic remain weak but have shown improvement. Inflation has risen, largely reflecting transitory factors. Overall financial conditions remain accommodative, in part reflecting policy measures to support the economy and the flow of credit to U.S. households and businesses.

The path of the economy will depend significantly on the course of the virus. Progress on vaccinations will likely continue to reduce the effects of the public health crisis on the economy, but risks to the economic outlook remain.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With inflation having run persistently below this longer-run goal, the Committee will aim to achieve inflation moderately above 2 percent for some time so that inflation averages 2 percent over time and longer-term inflation expectations remain well anchored at 2 percent. The Committee expects to maintain an accommodative stance of monetary policy until these outcomes are achieved. The Committee decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time. In addition, the Federal Reserve will continue to increase its holdings of Treasury securities by at least \$80 billion per month and of agency mortgage-backed securities by at least \$40 billion per month until substantial further progress has been made toward the Committee's maximum employment and price stability goals. These asset purchases help foster smooth market functioning and accommodative financial conditions, thereby supporting the flow of credit to households and businesses.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

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