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FOMC Announcement

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- The Fed delivered the highly anticipated quarter point rate hike, and at least in the text of its statement, didn't opt to signal a pause or give any solace to markets that are pricing in rate cuts for the second half of the year. The statement retained its prior wording that referred to the need for "ongoing increases" in rates ahead, which given the use of the plural term "increases", would seem to imply that there's more than one hike to come. There was a slight change to the wording around future hikes, with the "extent" of future increases depending on cumulative tightening, rather than the "pace", although that might be nothing more than reflecting the fact that having changed the "pace" to 25 bps, they were unlikely to go back to larger steps.
- While that was, if anything, a hawkish statement, Powell muddied the waters so much in his press conference that yields ended up lower. That's despite the fact that the market was already pricing in rate cuts in the back half of the year, and Powell expressed his personal view that he did not see that happening.
- The dovish tone came in remarks on inflation, where he had to acknowledge that the process of disinflation had begun, even though labor market slack has not yet materialized. Still, he emphasized that disinflation is coming from goods sectors (with housing set to join later in the year), and that policymakers need to see disinflation in core non-housing services to be confident about a sustainable return to on-target inflation. To get that, labor demand and supply have to come into balance, with recent readings on job openings (which jumped in the today's data), the unemployment rate, and wage growth still indicating a labor market that's too tight.
- Powell did seem much less sure of himself, perhaps reflecting diverging views on the FOMC, in terms of the near term path for rates, to some extent undermining the text of the statement that referred to "ongoing increases". Powell emphasized uncertainty from here to the May meeting, and data dependency could result in the fed funds rate heading higher than its December projection, or if the data come in in the other direction, perhaps diverging in the other direction.
- That opens to door to what we expect to see, which is a further quarter point hike in March, but no further moves beyond that, as inflation continues to melt away and give the Fed elbow room to allow a less punishing path for the economy. But we share Powell's view that an outright easing in rates in 2023 is less likely than the market expects, since we will need to see a bit of economic slack open up to assure the central bankers that having decelerated in 2023, inflation won't reaccelerate as the economy picks up in 2024.

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