mni

All Signal, No Noise

MARKET ANALYSIS

# MNI Fed Preview: June 2021

**Meeting Dates:** Tue-Wed, 15-16 June
**Decision/Statement/Summary of Econ Projections:** Wed 16 June at 1400ET / 1900BST
**Press Conference/Q&A:** Wed 16 June at 1430ET / 1930BST

**Minutes:** Wed 7 July

**Links (likely URLs based on previous meetings):**
- **Statement:** https://www.federalreserve.gov/newsevents/pressreleases/monetary20210616a.htm
- **SEP/Dot Plot:** https://www.federalreserve.gov/monetarypolicy/fomcprojtabl20210616.htm
- **Implementation note (if applicable):** https://www.federalreserve.gov/newsevents/pressreleases/monetary20210616a1.htm
- **Press Conference:** https://www.federalreserve.gov/monetarypolicy/fomcpresconf20210616.htm

**MNI Review of Previous FOMC (Apr):** https://roar-assets-auto.rbl.ms/documents/9721/FedRev-Apr2021.pdf

# Contents

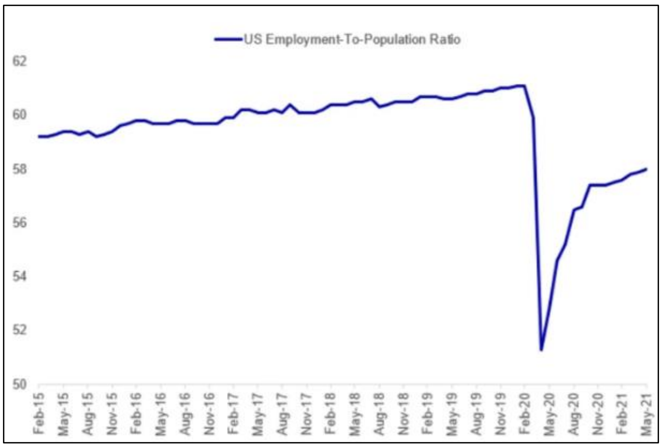


## MNI POV (Point Of View): Some "Talk", But Too Early To Act

*By Tim Cooper*

- The FOMC is likely to begin "talking about talking" about tapering at its June meeting.
- But Chair Powell will make clear that the FOMC is not yet ready to move any further than that on reducing asset purchases, with the recent jump in inflation being only "transitory", and weaker-than-expected job growth leaving the Fed far away from achieving its "substantial further progress" criteria.
- The 2023 Fed funds rate dots in the SEP are likely to show further support for a hike, with a good chance the median rises. The outlook for "transitory" inflation will also be eyed in the projections.
- The Fed is likely to hold off on tweaking the IOER and ON RRP rates (though prevailing analyst consensus is that this is a very close call).

**Taper Talk To Be More Of A Drip Feed:** FOMC communications since the April meeting have pointed toward a modestly hawkish shift in the Fed's outlook as the US economy continues to recover from the pandemic. The April FOMC minutes' commentary that "a number of participants" saw it "might be appropriate at some point in upcoming meetings to begin discussing a plan for adjusting the pace of asset purchases" provided ample cover for several participants to mention in public comments that they expected such a discussion to occur soon: this ranges from the more hawkish (Dallas' Kaplan) to the more dovish (SF Fed's Daly) regional presidents, all the way up to the Board of Governors (Vice Chair Clarida).



**But the minutes – and those participants - also made clear** that such a discussion would only be appropriate "if the economy continued to make rapid progress toward the Committee's goals". Such progress has not been clearly defined, and it's likewise clear that most participants haven't seen what they need to see yet. NY Fed President John Williams on June 3 likely summed up the Fed leadership's current thinking on "talking about talking" about tapering (in language that we could see repeated in Powell's press conference Wednesday):

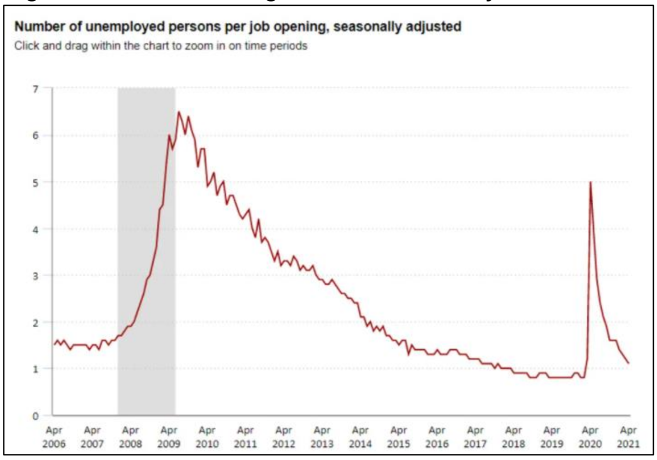
> *"We set that marker of substantial further progress back at the end of last year, and obviously, the economy has improved. I think it's on a good trajectory, but to my mind we're still quite a ways off from reaching the substantial further progress that we're really looking for in terms of adjustments to our asset purchase program. That said, we have to be thinking ahead, planning ahead, and so I do think it makes sense for us to be thinking through the various options that we may have in the future."*

**In other words, the June FOMC is likely to kick off the process** of weighing options and technicalities for the eventual taper so that they are prepared to move when "substantial further progress" is nigh. A timeline for a fairly expedient taper could look something like this:

- technical discussion around taper options at the July FOMC
- agreeing a general framework for tapering at / around the Jackson Hole symposium in August
- sufficient incoming (and less volatile) data by the September FOMC to begin signalling that they're getting toward "substantial further progress"
- formal taper announcement by December/January, with tapering beginning early 2022

This would be roughly in line with our Policy Team's reporting, which cites ex-Fed economists as saying the FOMC/Powell might not have enough evidence of a truly robust labor market by Jackson Hole to deliver a signal of an imminent QE taper at that point (**see our Policy section at the end of this preview**). He may deliver some more clarity on tapering criteria, but not more, as it would still be too early to gauge economic progress.

**Too Soon To Tell On Employment:** The employment outlook has been clouded since the last meeting by April and May jobs reports delivering weaker-than-expected results falling far short of a "string" of robust monthly readings (+559k in May, +278k in April). And for every metric that FOMC members bring up that suggest that labor market slack is dissipating and lower than the headline employment figures suggest, there is at least one other metric that signals a long and slow path back to full employment. Take two examples:

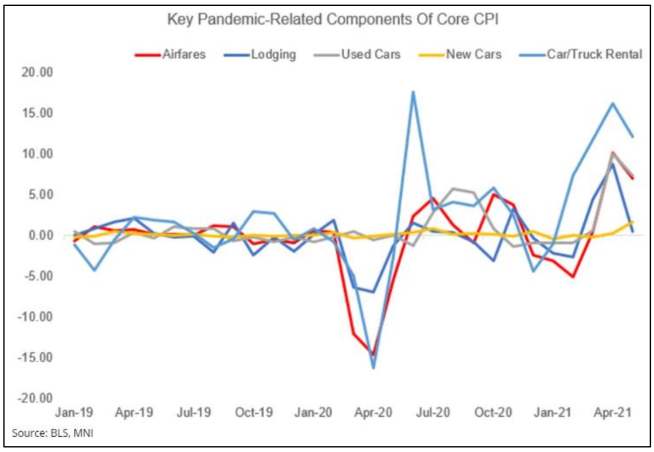



St Louis Fed Pres Bullard may well be bringing the chart opposite from the JOLTS report to the FOMC table, as he has claimed (<u>including in an MNI Interview last month</u>) the "unemployed-to-job opening" ratio is indicative of a much tighter labor market than headline unemployment stats would suggest. By this metric (1.1 unemployed people per opening), the labor market's getting close to as "tight" as it was pre-COVID (0.8 in Feb 2020), and below the pre-GFC lows (1.4).

Alternatively: Richmond Fed Pres Barkin said in May in reference to "substantial further progress" in meeting the Fed's full employment mandate that he was "closely tracking" the employment-to-population ratio, and was looking for a return to the pre-pandemic level (61.1% in Feb 2020) as a sign labor markets had recovered. But as the May employment report, that ratio has only edged higher 0.1pp in each of the last two months, and 0.6pp total in 2021 so far, to 58.0 in May (**see front page**). At a 0.1pp monthly pace of gains it would take 2-3 years to get to 61+%.

With demand for labor apparently strong (as seen in surveys and wage growth), supply-side labor issues are clearly weighing on jobs growth. But no matter one's view on whether these shifts are very temporary or longer-lasting, getting a signal from this noise will likely require at least 3 more jobs reports as well as the end of various factors that appear to be weighing on supply to end (including schools restarting and unemployment benefits expiring in the autumn). **That means it's likely the Fed will be very patient before it communicates any major shift in asset purchase policy.**

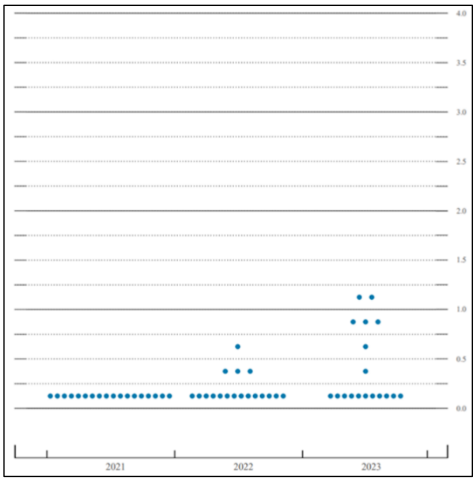
**Market Sees Inflation As Transitory…For Now:** Recent inflation readings may have given even the biggest "transitory inflation" proponents on the FOMC a jolt, with month/month rises (incl 0.9% in core CPI in April and 0.7% in May) suggesting it's not just a base effect generating huge Y/Y inflation numbers. But the market has given the Fed a huge reprieve in this regard. Rather than selling off further, bond yields have fallen sharply since the end of March, including a big drop in the wake of the May inflation report last week. And importantly, FOMC officials point to market expectations as being well-anchored: 5-Yr implied breakevens are where they were in early March (mid 2.40% area, well off the 2.76% recent peak), and 5Y5Y forwards remain below 5-Yr breakevens (Bullard has pointed to this as a sign inflation expectations haven't become entrenched).




That reprieve appears to reflect a view that the short-term spike is indeed re-opening related and unlikely to persist – Barclays for instance estimates that absent volatile categories, May headline and core CPI would have risen by just under 0.3%. This outlook may yet prove incorrect, particularly if some heretofore weak price categories pick up steam (e.g. shelter), but as with employment – it's just too early to tell. For the time being, it's enough to believe that the Fed itself will regard inflation as transitory.

**2023 Dot Hike Looking Likely:** Apart from any further developments on tapering, the most closely-watched element of the June meeting will be the updated Summary of Economic Projections. The macroeconomic Projections are due an update based on incoming data, and markets will be particularly sensitive to any further expectations of rate hikes by the end of the forecast horizon in 2023.

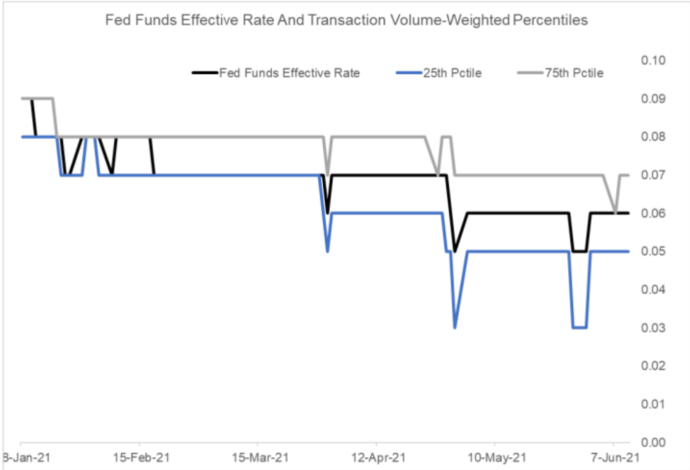
The March dot plot (**see chart to the right**) saw 4 of 18 participants seeing rates rising by end-2022; and 7 of 18 by end-2023. It would take only 2 FOMC members to shift to 'hike' to see a half-hike (0.25%) median for 2023, and 3 to move to a full 25bps hike. This might not present a major surprise to markets which are already pricing in a rate hike cycle beginning in 2023, but it will help reinforce the steadily-more-hawkish-Fed narrative. A 'no hike' median could be perceived dovish, particularly in the context of higher inflation projections (see next section). Also important are the 2022 dots: it's possible - if unlikely - more FOMC members join the call for earlier hiking. One more hiking dot that year would probably be taken in stride, but two or more would spur speculation that the median could shift higher as soon as the September meeting.




**Watch The 2021 vs 2022 Inflation Projections For "Transitory" Effect:** Inflation revisions will be the most closely watched among the new macroeconomic forecasts. The core PCE projection of 2.4% in 2021 will be revised firmly higher due to much higher-than-expected readings for April and May. A 2.7-3.0% 2021 expectation wouldn't be seen as much of a shock, though the trajectory through 2023 is equally important. In particular for 2022, any revision much higher than 2.1% (vs 2.0% in the March SEP) would call into question how "transitory" the FOMC really sees the current rise in inflation.

**GDP And Unemployment Unlikely To Change Much:** The GDP growth forecast may be revised up on a mark-to-market basis for 2021 (closer to 7.0% on a Q4/Q4 basis than the 6.5% in the March projection), though may not be substantially different for 2022 and 2023. The 4.5% end-2021 unemployment rate may be due a modest adjustment higher given weaker-than-expected jobs growth so far, but likewise there's probably little need to change this substantially given expectations that employment will pick up in H2.

**IOER / ON RRP Hikes Not A Done Deal:** Despite continued evidence of rising reserves putting downward pressure on overnight rates, most analysts see a Fed adjustment of administered rates this month as a close call. Prevailing opinion on whether the Fed will act appears to be shifting toward an expectation of inaction, as the funds rate remains at 0.06% (despite a brief dip to 0.05%) – but a small majority of sell-side analysts expect the Fed to adjust administered rates (potentially raising both IOER and ON RRP rates) at the June Fed meeting. By our count, of 18 analysts who expressed an opinion, 9 saw an adjustment coming this week, with 6 "no's" and 3 on the fence. Per our Policy Exclusive **("Fed IOER Hike On Hold Unless Debt Limit Talks Drag On"**, see our policy section), tweaks look to have been parked for now, with officials only likely to move if negotiations over the debt limit drag on into the fall, current and former officials told MNI.




# MNI Instant Answers:

**The questions that we have selected for this meeting are:**

- Changes to Fed Funds / Interest Rate Paid on Excess Reserves (IOER) / ON RRP?
- Does the Fed announce changes to asset purchases with regard to size, duration, and/or Tsy vs MBS?
- How many 'dots' imply higher rates by end-2022? End-2023?
- 2021, 2022 and 2023 core PCE inflation medians?
- Does the Fed announce the creation of a standing repo facility?
- Any dissents to the decision?

*(Formerly Human Readable Algo) The markets team have selected a subsection of questions we think could be most market moving and will publish the answer to all of these questions within a few seconds of the Fed statement being released. These questions are subject to change; clients will be informed of any changes via our Edge and Bullets services.* **A comprehensive list of questions is available on the MNI Monitor (available via the website here:** https://www.marketnews.com/realdisplay?product=AFM

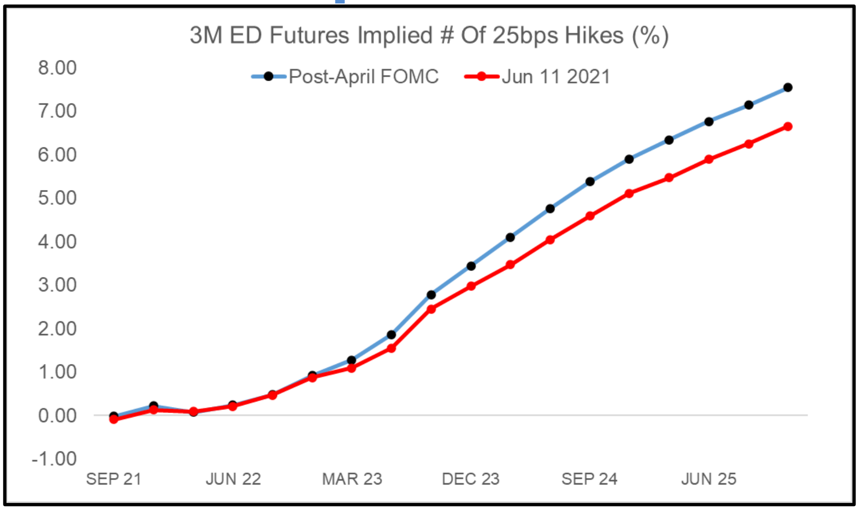
# Analyst Views – Fed Outlook

- **While no analysts expect any substantial change in policy at the June FOMC,** most expect that participants will initiate early discussions on tapering, but falling well short of signalling any imminent action. Whether that's communicated at the press conference or in the meeting minutes is a matter of debate.
- The Dot Plot is expected to show a median hike to be introduced in 2023, though opinion is split: some see no change; see the median shifting to 0.25% (2 dots move up), some see 0.375%, and one (Credit Suisse) sees a 50bps rise to the median as possible.
- Broad sell-side consensus hasn't changed much since the April FOMC: asset purchase tapering is expected to will begin by early 2022, with Fed funds rate hikes not before mid 2023.
- The most significant forecast change is JPM moving their rate hike timing to late 2023 (was 2024).
- ***For a summary of analysts` individual notes, please see pages 12-19.***

| Analyst | Timing Of Beginning Of Taper | Fed Funds Rate Liftoff |
|---|---|---|
| **Citi** | Dec 2021 FOMC | |
| **UBS** | Jan 2022 | 2024 |
| **ING** | Announcement Dec FOMC | 2023 |
| **Deutsche** | Dec 2021 FOMC | 2Q 2024 |
| **JPMorgan** | Announced by end-2021 | **Late 2023 (was 2024)** |
| **HSBC** | By end-2021 | Not until at least 2023 |
| **BMO** | Announced Sep 2021 | Mar 2023 |
| **Morgan Stanley** | Starting Apr 2022 | |
| **BofA** | Early 2022 | 2H 2023 |
| **Danske** | Jan 2022 | 1Q 2023 |
| **SocGen** | Early 2022 | |
| **Scotiabank** | Early 2022 | |
| **ABNAMRO** | Early 2022 | 2023 (2 or 3 hikes over 2023-24) |
| **Goldman Sachs** | Early 2022 | Mid-2023 |
| **NatWest** | 2022 | 2024 |
| **Nomura** | Early 2022 | 3Q 2023 |
| **SEB** | Decision in Nov, Beginning Dec 2021 | Not until at least end-2022 |
| **Swedbank** | Dec 2022 | |
| **Unicredit** | Q1 2022, concluding early 2023 | Late 2023 |
| **BNPParibas** | 1H 2022 | 2H 2023 |
| **Wrightson ICAP** | Late 2021/Jan 2022 | |
| **Wells Fargo** | Not before End-2021 | Not before 2023 |
| **TD** | Starting Mar 2022 | 2024 |

*Correct to the best of MNI`s knowledge as of Jun 14*

# Market-Implied Rate Outlook




*Source: Bloomberg, MNI Market News*

- Fed liftoff expectations have moderated since the April FOMC: we now estimate the first hike is only fully priced by March 2023, whereas in late April it was seen no later than the Dec 2022 meeting. Roughly one full 25bp hike has been brought out of the rate path to Dec 2025 (by which point around 6.5 cumulative hikes are seen, vs 7.5 just after the Apr FOMC). (*Updated Jun 11)*

## mni Central Bank Watch - FED

### MNI FED Data Watch List

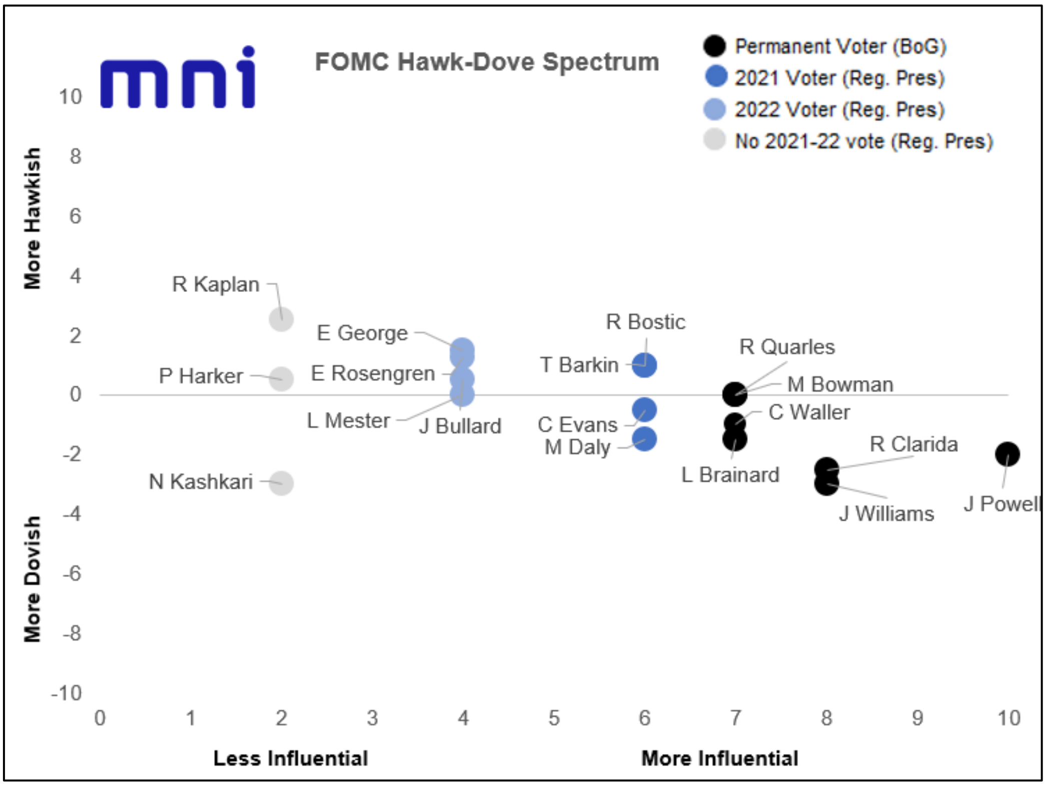
| Inflation | | Current | 3m ago | 3m Chg | 6m ago | 6m Chg | 2Y History | Hit / Miss | Vs Trend | Surprise Index | Z-Score |
|---|---|---|---|---|---|---|---|---|---|---|---|
| CPI | % y/y | 5.0 | 1.7 | ↑ | 1.2 | ↑ | | | | | 3.00 |
| PCE Deflator | % y/y | 3.6 | 1.4 | ↑ | 1.2 | ↑ | | | | | 2.17 |
| UoM 1-Yr Inflation Exp | % y/y | 4.0 | 3.1 | ↑ | 2.5 | ↑ | | | | | 0.98 |
| Inflation Swap 5y/5y | % | 2.38 | 2.23 | ↑ | 2.24 | ↑ | | | | | 1.16 |
| **Economic Activity** | | **Current** | **3m ago** | **3m Chg** | **6m ago** | **6m Chg** | **2Y History** | **Hit / Miss** | **Vs Trend** | **Surprise Index** | **Z-Score** |
| ISM | Index | 61.2 | 60.8 | ↑ | 57.7 | ↑ | | | | | 1.30 |
| Industrial Production | % m/m | 0.55 | 1.00 | ↓ | 1.09 | ↓ | | | | | 0.09 |
| Factory Orders | % m/m | -0.6 | 2.3 | ↓ | 0.9 | ↓ | | | | | -1.89 |
| Housing Starts | K | 1569 | 1625 | ↓ | 1514 | ↑ | | | | | 0.00 |
| **Monetary Analysis** | | **Current** | **3m ago** | **3m Chg** | **6m ago** | **6m Chg** | **2Y History** | **Hit / Miss** | **Vs Trend** | **Surprise Index** | **Z-Score** |
| Corporate Spreads BBB/Baa | bps | 1.08 | 1.10 | ↓ | 1.19 | ↓ | | | | | -0.95 |
| Chicago Fed Financial Con | Index | -0.71 | -0.64 | ↓ | -0.59 | ↓ | | | | | -1.09 |
| Consumer Credit Net Chg | $bn | 18.6 | -5.7 | ↑ | 0.4 | ↑ | | | | | 0.79 |
| New Home Sales | K | 863 | 993 | ↓ | 969 | ↓ | | | | | -1.06 |
| **Consumer / Labour Market** | | **Current** | **3m ago** | **3m Chg** | **6m ago** | **6m Chg** | **2Y History** | **Hit / Miss** | **Vs Trend** | **Surprise Index** | **Z-Score** |
| Retail Sales | % m/m | 0.0 | 7.6 | ↓ | 0.1 | ↓ | | | | | -0.16 |
| Consumer Confidence | Index | 117.2 | 95.2 | ↑ | 92.9 | ↑ | | | | | 1.18 |
| Nonfarm Payrolls Net Chg | K | 559 | 536 | ↑ | 264 | ↑ | | | | | 0.52 |
| Average Hourly Earnings | % y/y | 2.0 | 5.2 | ↓ | 4.5 | ↓ | | | | | -1.08 |
| **Markets** | | **Current** | **3m ago** | **3m Chg** | **6m ago** | **6m Chg** | **2Y History** | **Hit / Miss** | **Vs Trend** | **Surprise Index** | **Z-Score** |
| Equity Market | Index | 4238 | 3811 | ↑ | 3622 | ↑ | | | | | 2.04 |
| US 10-Year Yield | % | 1.47 | 1.40 | ↑ | 0.84 | ↑ | | | | | 0.90 |
| US Yield Curve (2s-10s) | bps | 131.6 | 127.8 | ↑ | 69.0 | ↑ | | | | | 0.91 |
| USD TWI | Index | 90.82 | 92.70 | ↓ | 91.63 | ↓ | | | | | -0.80 |

- Inflation is hitting multi-year highs, and while nonfarm payroll growth has been strong, it has surprised to the downside and well off the pace required to recover jobs lost in the pandemic. Notably, output has suffered from bottleneck / supply chain issues, as seen in industrial production and housing starts. (*Updated Jun 11)*

# Key Inter-Meeting FedSpeak – Jun 2021

**Here are the prevailing FedSpeak themes since the April FOMC:**

- It's become clearer since the April meeting that a growing (and increasingly influential) group within the FOMC expect a discussion on tapering asset purchases to begin soon.
- This was underlined by the April minutes which included "a number of participants suggested that if the economy continued to make rapid progress toward the Committee's goals, it might be appropriate at some point in upcoming meetings to begin discussing a plan for adjusting the pace of asset purchases".
- Several FOMC members have said in the inter-meeting period (and notably, since the April inflation report) that discussion will soon / should soon begin: a list including regional presidents (Kaplan, Harker, Daly, Mester, Bullard), but also some board members (Clarida, Quarles).
- Multiple Fed speakers underlined that the spike in April / May inflation data was transitory and driven by temporary effects, and should normalize in 2022 and beyond. Several emphasized monitoring inflation expectations, with Brainard calling them "extremely" well-anchored.
- The message on weaker-than-expected employment data has been slightly more mixed. FOMC members continue to see the labor market as continuing to lag the Fed's goals, though expect employment growth to pick up as the year progresses and supply issues dissipate. However, some have emphasized signs that the labor market is tighter than it looks on the surface (Bullard).
- We've highlighted comments made on tapering mortgage-backed securities before/more quickly than Treasuries: several FOMC members mentioned this as likely part of the taper discussion as a whole.




*Our matrix uses the following methodology based on the MNI Markets Team`s subjective analysis. **Hawkish/Dovish scores** indicate MNI`s subjective assessment of each member`s stance on monetary policy. -10 implies member believes aggressive easing warranted; +10 is most hawkish, implies member believes aggressive tightening warranted. Scores around -2 to +2 considered relatively neutral. On **Influence**, the x-axis runs from 0 ('least influential') to 10 ('most influential'). Voters in the current year receive a minimum score of 6; the Chair receives a 10 and Board of Governors members receive at least 7. Those who are not voters in the current year are limited to a score of 4; among them, those due to vote next year receive higher influence scores (rising towards end of current year), and vice-versa.*

| Member | Role | Voter | | Monetary Policy Commentary Since April FOMC |
|---|---|---|---|---|
| | | '20 | '21 | |
| **J Powell** | BOG, Chair | **X** | **X** | **On the economic outlook:** "The economy is reopening, bringing stronger economic activity and job creation… We are not out of the woods yet." **– May 3** |
| **J Williams** | NY Fed, V Chair | **X** | **X** | **On the economic outlook**: "In the end, we're going to get to a full, strong recovery, and that's what's important…[but] "we're in an extraordinary period of supply and demand -- both supply and demand moving very quickly." **– May 5**<br>"I expect GDP growth this year to be the fastest in decades. Specifically, I see inflation-adjusted, or real, GDP increasing around 7% this year." **– May 4**<br>**On tapering:** "The economy has improved, and I think it's on a good trajectory, but to my mind, we're still quite a ways off from reaching the 'substantial further progress' that we're really looking for, in terms of adjustments to our purchases…. That said, we have to be thinking ahead, planning ahead, and so I do think it makes sense for us to be thinking through the various options that we may have in the future -- talking about talking about how the economy is doing, where we see it going, and understanding how that may play out over the coming months." **-Jun 3**<br>**On inflation:** ""My personal view is that a big chunk of the increase in the inflation measures that we've seen is partly this reversal of price declines from before -- what we often call base effects -- plus some special factors like used cars." **-Jun 3** |
| **R Clarida** | BOG | **X** | **X** | **On the economic outlook:** "The most recent employment report really highlights a fair amount of near-term uncertainty about the labor market. I myself think that the pace of labor-market improvement will pick up." **– May 25**<br>**On tapering:** "It may well be [that] in upcoming meetings, we'll be at the point where we can begin discuss scaling back the pace of asset purchases. I think it's going to depend on the flow of data that we get." **– May 25**<br>- "In my judgment, through that April employment report, we have not made substantial further progress…. [Tapering to have] more of a focus on the labor market." **-May 17**<br>**On inflation:** "Obviously the [April] CPI number that we got recently was a very unpleasant surprise. We and other forecasters had expected both PCE and CPI inflation to move up on reopening but that increase certainly caught my eye and others' attention, I continue to believe as my baseline case that this will prove to be largely transitory and I think the details of that recent report are consistent with that, but let me also emphasize, we're going to be looking at the data very closely in coming months." **– May 25** |
| **L Brainard** | BOG | **X** | **X** | **On the economic outlook:** "Today employment remains far from our goal… it appears that labor supply is lagging behind labor demand in several sectors, in part reflecting ongoing concerns about the virus and caregiving responsibilities" **- Jun 1**<br>**On inflation:** "While the level of inflation in my near-term outlook has moved somewhat higher, my expectation for the contour of inflation moving back towards its underlying trend in the period beyond the reopening remains broadly unchanged…I am attentive to the risks on both sides…I will carefully monitor inflation and indicators of inflation expectations for any signs that longer-term inflation expectations are evolving in unwelcome ways"**-Jun 1**<br>"A very important part of inflation dynamics is longer-term inflation expectations and those have been extremely well anchored, implying that if we saw some development pushing inflation up I wouldn't expect that to get embedded in the ongoing inflation rate." **-May 24**<br>**On monetary policy:** "Remaining steady in our outcomes-based approach during the transitory reopening surge will help ensure the economic momentum that will be needed as current tailwinds shift to headwinds is not curtailed by a premature tightening of financial conditions. The best way to achieve and sustain our maximum-employment and average-inflation goals is by remaining steady and clear in our approach while also being attentive to changing conditions." **- Jun 1** |
| **R Quarles** | BOG | **X** | **X** | **On the economic outlook:** is "quite optimistic...rapid growth to continue for some time before slowing to a still robust pace next year." **– May 25**<br>**On inflation:** "My personal view is that the rise in inflation—even after discounting temporary factors—and inflation expectations since December will prove sufficient to satisfy the standard for inflation in the guidance around asset purchases later this year, but improvement in the labor market has been slower than I would have liked…. I expect inflation to begin subsiding at some point over the next several months and to be running close to 2 percent again at some point during 2022." -May 26<br>**On tapering:** "If my expectations about economic growth, employment and inflation over the coming months are borne out….and especially if they come in stronger than I expect, then…it will become important for the FOMC to begin discussing our plans to adjust the pace of asset purchases at upcoming meetings. In particular, we may need additional public communications about the conditions that constitute substantial further progress since December toward our broad and inclusive definition of maximum employment." -May 26<br>**On monetary policy:** "In contrast, the time for discussing a change in the federal funds rate remains in the future." -May 26<br>**On MBS purchase policy:** "We'll be certainly looking at it as we consider our asset purchase policy generally." – May 25 |
| **M Bowman** | BOG | **X** | **X** | **On the economic outlook:** "At our March meeting, my view was broadly in line with the median of projections of other members of the FOMC…But the outlook has improved since then… We really can't know how the pandemic will proceed and how that will affect the U.S. economy, but I think we are currently on a good path, and our policy is in a good place." **– May 5** |
| **C Waller** | BOG | **X** | **X** | **On the economic outlook:** "We need to see several more months of data before we get a clear picture of whether we have made substantial progress towards our dual-mandate goals." **– May 13**<br>**On inflation:** "I expect that [supply issues etc] will cause inflation to overshoot our 2 percent longer-run goal in 2021. But they will not lead to sustained, high rates of inflation… Our willingness to aim for above-target inflation |

| Member | Role | Voter | | Monetary Policy Commentary Since April FOMC |
|---|---|---|---|---|
| | | ‘20 | ‘21 | |
| | | | | also means we will not overreact to temporary overshoots of inflation—we need to see inflation overshoot our target for some time before we will react…[The April CPI report] was a surprise, but a look at its causes doesn’t alter my fundamental outlook, which is that the main pressures on inflation are temporary.” **– May 13** |
| **C Evans** | Chic. Fed | | **X** | **On inflation:** “It is important to emphasize that the recent increase in inflation does not appear to be the precursor of a persistent movement to undesirably high levels of inflation.” **– May 25**<br>“To average 2% you’ve got to be above 2% for some period of time…so inflation rates of 2.5% don’t bother me as long as it’s consistent with averaging 2% over some period of time.” **– May 10**<br>“I would not be concerned about inflation moving persistently too high unless we saw some quite outsized movements in financial market pricing at the longer maturities or in survey-based measures of inflation expectations." **– May 5**<br>**On tapering:** “I have not seen anything yet to persuade me to change my full support of our accommodative stance for monetary policy or our forward guidance about the path for policy.” **– May 25**<br>(re substantial further progress): “I think we want to be headed to an unemployment rate that is headed towards 4% and below that. It’ll be a while…In the current environment we’re looking for employment to continue to grow month after month. I think we’re looking for a couple of those million a month employment reports.” **– May 10** |
| **T Barkin** | Rich. Fed | | **X** | **On the economic outlook:** “The supply-chain and workforce challenges look to last into the summer…There is still a lot of room to grow in the labor market, it will take until the summer to unclog this.” **– May 25**<br>"Have we made progress in the economy since January? The answer is yes…[that] puts us closer to substantial further progress.” **– May 21**<br>**On inflation:** “I pay attention to market measures of inflation expectations, and those have not yet escalated over target.” **– May 25**<br>**On monetary policy/tapering**: “I’m not ready at this point to completely pivot. I do want to see a lot more job creation before I’m willing to push on this too hard.” **– May 21**<br>[April job growth] “is nowhere near as strong as I expected and I think as most commentators expected given the surge in demand… “I am looking for substantial further progress on that metric [employment-to-population ratio]. I had hoped to see an even stronger report today than we saw, so we’ll see where we go on that.…We’re making I think real progress on the inflation side…I am feeling pretty positive on that” **– May 7** |
| **R Bostic** | Atl. Fed | | **X** | **On the economic outlook:** “I’m expecting a lot of volatility over the next several months…" We're going to have to be very nimble in terms of our monitoring of the economy and our policy responses.” -**May 19**<br>**On inflation:** “I am not seeing that it is going to be enduring…the demand response has been much faster than supply responses” **– May 24**<br>**On tapering**: “If we see that substantial, significant progress towards our goals, I am going to be advocating for us moving policy…we are not there right now..we’re still 8 million jobs short. We have not had the sustained levels of inflation above our target that we are looking for.” **– May 19**<br>**On MBS purchase policy:** “I think that’s something we’re definitely going to have to think about.” **– May 19** |
| **M Daly** | S.F. Fed | | **X** | **On the economic outlook:** “My modal outlook is quite positive; I’m bullish about where the economy will be at the end of the year.” **– May 11**<br>“There’s just going to be a sequence of these temporary factors that are going to persist probably through the end of the year… They will start to roll off at the beginning of next year. How many of them will roll off or whether other bottlenecks will emerge as we start to get the economy back into shape and get back into recovery is hard to say.” **– May 21**<br>**On tapering:** “We’re talking about talking about tapering, and that is what you want out of us. You want to be long-viewed here…but I want to make sure that everyone knows it’s not about doing anything new. Right now, policy is in a very good place. Policy is supporting the American people.” **– May 25** |
| **P Harker** | Phil Fed | **X** | | **On tapering:** “I think it is appropriate for us to slowly, carefully move back on our purchases at the appropriate time. When that is, that is something we need to start discussing…We have to be careful in removing accommodation so that we don’t create any kind of ‘taper tantrum’. And that’s why we need to communicate very early, very often what we’re going to do.” **– Jun 2**<br>“It is something that, in my mind, we should start to have a conversation about sooner rather than later.” **– May 21**<br>“What I’m looking for, in terms of when we start that process, is continued strength in the labor market [ and inflation above 2% for a period of time]…if I see those things starting to happen, then yeah, I think it’s appropriate that we start the tapering discussion.” **-May 21** |
| **R Kaplan** | Dall. Fed | **X** | | **On the economic outlook:** “Policy makers should be cognizant of a range of supply factors that may currently be weighing on employment. These factors may not be particularly susceptible to monetary policy…We would expect that many of these factors will fade as the year progresses, increasing the number of job seekers and potentially reducing labor-market tightness” **– May 27**<br>**On tapering:** “You don’t want to be so preemptive that you choke off the recovery. But on the other hand you don’t want to be so reactive you’re late and you’re behind the curve…we need to telegraph well in advance. Give the markets plenty of notice. And I think we should be doing this -- when we do start to adjust purchases -- do it in a gradual way…My job is not to put a label on it or to know exactly the outcome. But it is to be open to a range of outcomes and manage the risk, understanding our commitment is to anchor inflation expectations at 2%.” **– May 27**<br>**On MBS purchase policy:** “I think at this stage, as it’s clear we’re weathering the pandemic and making progress, I don’t think the housing market needs the level of support that the Fed is currently providing and I would love to see, sooner rather than later, a discussion of the efficacy, for example, of those mortgage purchases.” **– Jun 3** |

| Member | Role | Voter '20 | Voter '21 | Monetary Policy Commentary Since April FOMC |
|---|---|---|---|---|
| N Kashkari | Minn. Fed | X | | **On the economic outlook:** "Today, roughly eight million Americans are out of work who were working before the pandemic. I assume that those folks want to work again…how long is it going to take to bring all of those folks back into the labor market and really achieve full employment? We'll see. It may take a few years." **– May 5**<br>**On inflation:** "Right now, there's a big debate happening in economic circles about: Is the economy overheating? With all of this fiscal stimulus, are these higher inflation readings here to stay or not? "I don't think they are here to stay because I believe we are going to bring women back into the labor force, and workers who have been displaced...But if we fail to do that, then these high inflation readings become a lot more concerning, because then it would signal we're overheating the economy." **- Jun 1**<br>**On monetary policy:** "If we need to raise rates, we'll do it, but let's not cut off the recovery prematurely." **– May 5** |
| L Mester | Clev. Fed | X | | **On the economic outlook:** "I view it [May nonfarms] as a solid employment report," she said. "But I'd like to see further progress." **– Jun 4**<br>**On inflation:** "My baseline scenario for inflation is we're going to have higher inflation this year, above 2%, but then as some of those constraints on supply ease I think we're going to see inflation go back down and we'll have to monitor that as we go forward." **- May 14**<br>**On tapering:** "We want to be very deliberately patient here because, you know, this was a huge, huge shock to the economy." **– Jun 4**<br>**On monetary policy:** "I think we're in a good place right now with our policy and we're going to adjust it as appropriate depending on how the actual recovery progresses… this is not the time to be adjusting anything on policy. It really is a time for watchful waiting, seeing how the recovery evolves." **- May 14** |
| E George | K.C. Fed | | | **On the economic outlook:** "I anticipate strong employment growth in the coming months, particularly in contact-intensive industries such as hospitality and live entertainment…as the pace and strength of the recovery unfolds, monetary policy settings remain highly accommodative and will remain so for some time in line with the FOMC's forward guidance." **– May 24**<br>**On inflation:** "While it is clear that several temporary factors are boosting inflation now, I am not inclined to dismiss today's pricing signals or to be overly reliant on historical relationships and dynamics in judging the outlook for inflation." **-May 24**<br>**On monetary policy:** "With a tremendous amount of fiscal stimulus flowing through the economy, the landscape could unfold quite differently than the one that shaped the thinking around the revised monetary policy framework…that suggests remaining nimble and attentive to these dynamics will be important as we seek to achieve our policy objectives…as the economy works its way towards a new equilibrium, policymakers will be well served to take a flexible approach to monetary policy decisions." **-May 24**<br>**On MBS purchase policy:** "It is a fair question to ask to what extent do those asset purchases differ than the Treasury purchases?...so I think that will have to be part of the discussion as we get into that and really think about what effect our purchases are having on broader financial markets." **– May 24** |
| E Rosengren | Bos. Fed | | | **On the economic outlook:** "While rapid economic growth is very good news, it was, and still is, badly needed to offset the sizable shock that occurred with the Covid-19 pandemic." **– May 5**<br>**On tapering:** "We need to have a substantial improvement for us to begin tapering. It is quite possible that we will see those conditions as we get to the end of the year." **– May 5**<br>**On MBS purchase policy:** "I do think that as we think about tapering one of the things that we are going to have to think about is at what speed we taper the Treasuries versus the mortgage-backed securities…my own personal view is that the mortgage market probably doesn't need as much support now. And in fact, one of my financial stability concerns would be if the housing market gets too overheated." **-May 5** |
| J Bullard | St. Louis Fed | | | **On the economic outlook:** "April was a little bit too early to expect really big jobs numbers…we've made a lot of progress so far and with this booming economy I think we're likely to move even further in the direction of a tight labor market." **– May 17 MNI Interview**<br>**On inflation:** "We were certainly expecting year-over-year comparisons to make the inflation number look hot -- that certainly happened [in the April CPI report]" Bullard told MNI. "I don't think that those are the kinds of lasting increases of prices that you would call inflation, but I do think it's enough to have sent inflation expectations somewhat higher." **– May 17 MNI Interview**<br>**On tapering:** "If we got to the point where we were comfortable on the public health side that the pandemic was largely behind us, and was not going to resurge in some way that was surprising, then I think we could talk about adjusting monetary policy...I don't think we're quite to that point yet, but it does seem like we're getting close." **– May 19**<br>**On monetary policy:** "I would like to see a more definitive end to the pandemic before we change monetary policy…the probabilities are rising probably to pretty high levels that it will come to an end. But you'd really like it to be more definitively finished than it is today and then at that point we can open up discussions as to where to go next…it's important for Jay [Powell] to open that discussion as opposed to members of the committee." **– May 17 MNI Interview** |

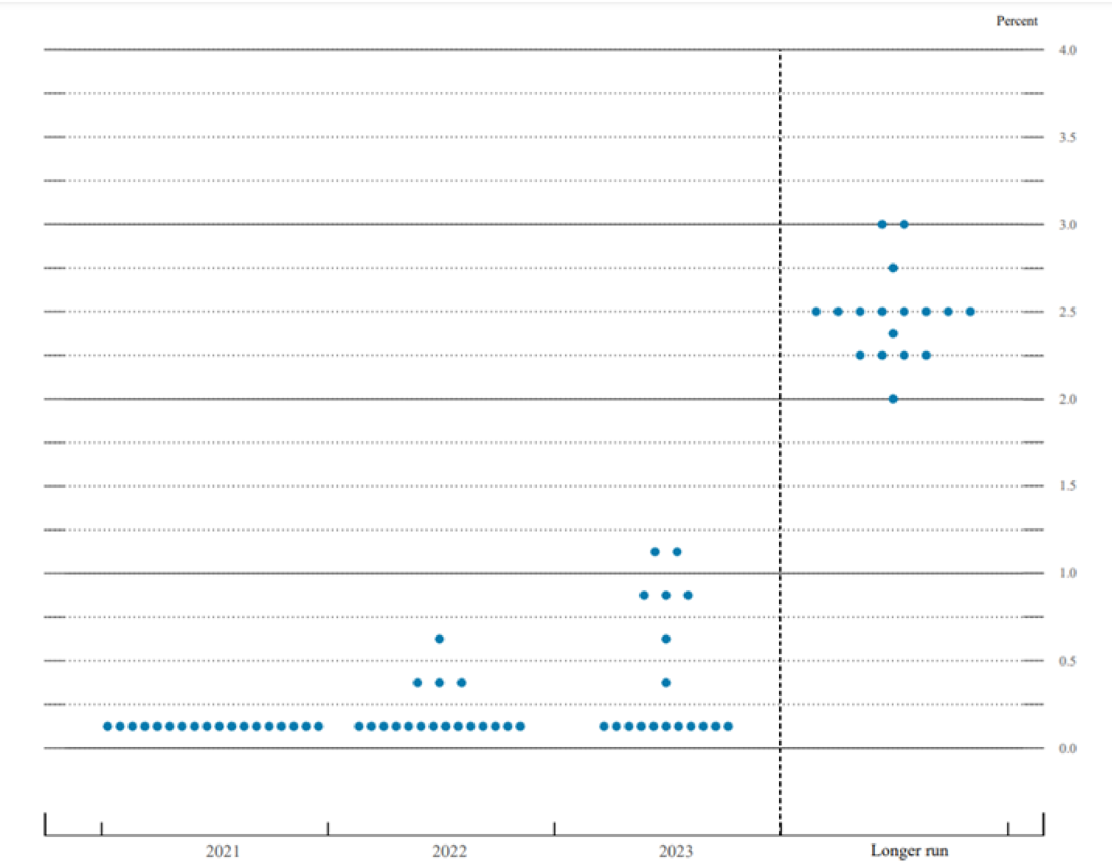
# Previous Dot Plot/SEP (Mar FOMC)

**MARCH 2021 FOMC: Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents, under their individual assumptions of projected appropriate monetary policy. Source: Federal Reserve**

Percent

| Variable | Median[1] | | | | Central Tendency[2] | | | | Range[3] | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2021 | 2022 | 2023 | Longer run | 2021 | 2022 | 2023 | Longer run | 2021 | 2022 | 2023 | Longer run |
| Change in real GDP | 6.5 | 3.3 | 2.2 | 1.8 | 5.8–6.6 | 3.0–3.8 | 2.0–2.5 | 1.8–2.0 | 5.0–7.3 | 2.5–4.4 | 1.7–2.6 | 1.6–2.2 |
| December projection | 4.2 | 3.2 | 2.4 | 1.8 | 3.7–5.0 | 3.0–3.5 | 2.2–2.7 | 1.7–2.0 | 0.5–5.5 | 2.5–4.0 | 2.0–3.5 | 1.6–2.2 |
| Unemployment rate | 4.5 | 3.9 | 3.5 | 4.0 | 4.2–4.7 | 3.6–4.0 | 3.2–3.8 | 3.8–4.3 | 4.0–5.5 | 3.2–4.2 | 3.0–4.0 | 3.5–4.5 |
| December projection | 5.0 | 4.2 | 3.7 | 4.1 | 4.7–5.4 | 3.8–4.6 | 3.5–4.3 | 3.9–4.3 | 4.0–6.8 | 3.5–5.8 | 3.3–5.0 | 3.5–4.5 |
| PCE inflation | 2.4 | 2.0 | 2.1 | 2.0 | 2.2–2.4 | 1.8–2.1 | 2.0–2.2 | 2.0 | 2.1–2.6 | 1.8–2.3 | 1.9–2.3 | 2.0 |
| December projection | 1.8 | 1.9 | 2.0 | 2.0 | 1.7–1.9 | 1.8–2.0 | 1.9–2.1 | 2.0 | 1.2–2.3 | 1.5–2.2 | 1.7–2.2 | 2.0 |
| Core PCE inflation[4] | 2.2 | 2.0 | 2.1 | | 2.0–2.3 | 1.9–2.1 | 2.0–2.2 | | 1.9–2.5 | 1.8–2.3 | 1.9–2.3 | |
| December projection | 1.8 | 1.9 | 2.0 | | 1.7–1.8 | 1.8–2.0 | 1.9–2.1 | | 1.5–2.3 | 1.6–2.2 | 1.7–2.2 | |
| Memo: Projected appropriate policy path | | | | | | | | | | | | |
| Federal funds rate | 0.1 | 0.1 | 0.1 | 2.5 | 0.1 | 0.1–0.4 | 0.1–0.9 | 2.3–2.5 | 0.1 | 0.1–0.6 | 0.1–1.1 | 2.0–3.0 |
| December projection | 0.1 | 0.1 | 0.1 | 2.5 | 0.1 | 0.1 | 0.1–0.4 | 2.3–2.5 | 0.1 | 0.1–0.4 | 0.1–1.1 | 2.0–3.0 |

**FOMC participants' assessments of appropriate monetary policy: Midpoint of target range or target level for the federal funds rate.** Source: Federal Reserve



# Analysts' Key Comments

**Note summaries in alphabetical order of institution. All analysts expect <u>no change</u> in the Funds rate at the June FOMC, but opinion varies on changes to other policy tools, particularly on asset purchases. Key abbreviations: Fwd Guidance = Forward Guidance; SEP = Summary of Economic Projections; IOER = Interest On Excess Reserves; ON RRP = Overnight Reserve Repo Facility Rate**

**ABNAmro: Taper Announcement Could Come As Soon As July**

ABN sees a taper announcement as having to wait for now, as "the general message from FOMC members has been that the current policy stance remains appropriate, that the economic outlook is strong, and that the recent rise in inflation is driven by temporary factors and is not a concern at this stage."

- **Future action:** Announcement on taper could come as soon as July or September, implying actual tapering starting in Q4. ABN's base case is tapering beginning early 2022.

**Barclays: FOMC To Sweat Out Summer Bottlenecks**

Barclays sees some early discussion of tapering at the June FOMC, but "reluctant workers slowing the employment recovery" mean a formal announcement is unlikely until late 2021.

- The discussion of whether there has been "substantial further progress" to be brief.
- **Statement:** Minor changes to acknowledge stronger activity, lagging employment, and inflation >2% and likely to remain so for a time due to transitory factors (with long-term expectations still anchored).
- **SEP/Dot Plot:** 2023 rate liftoff median, though "a close call".
- **Press conference:** Powell "to stick to the FOMC's narrative that recent inflationary pressures reflect transitory bottlenecks that are likely to ease as reopening proceeds, and that the labor market is still a long way from full employment."
- **Administered rates:** IOER and ON RRP rates boosted 5bp.

**BMO: A Tiny But Meaningful Tonal Tweak**

BMO sees "a faintly less ardent but still very accommodative tone" at the June FOMC, but suspects "the staff will be charged with briefing the Committee on tapering options and consequences for the July meeting".

- **Statement:** To again acknowledge economic/employment progress, and inflation accelerating due to transitory factors.
- **SEP/Dot Plot:** At least two more participants to indicate 2023 rate hike, enough to push up the median. Means to rise for both 2022 and 2023 as well.
- **Press conference:** Powell may indicate that tapering talk could begin soon.
- To emphasize that a median 2023 dot plot hike is a forecast and not a policy promise, and that higher rates due to strong growth and employment is a good thing.
- **Administered rates:** "Even odds" of an ON RRP / IOER increase.

**BNP Paribas: Thinking About Thinking**

BNP expects the Fed to use the June meeting to "try to maintain dovish forward guidance on rates while laying some groundwork on upcoming taper discussions and noting recent data volatility in employment and inflation".

- **SEP/Dot Plot:** Inflation and growth expectations to be upgraded, vs marginal downgrade for employment. Core PCE 2.5% 2021 median; unch for 2022-23.
- No hikes in median dot through 2023 (though perhaps one dot shifting from no-hike to hike).
- **Press conference:** Powell to emphasize the Fed is more focused on seeing job gains when weighing taper timing, but will be sanguine about near-term inflationary pressures. Would likely note evidence of supply constraints that will probably ease over the course of the year.

**BofA: Faith In The Patient Fed**

BofA sees the message from the Fed being "one of patience with an emphasis on outcome-based rather than outlook-based monetary policy". "This is not a Fed that is rushing to the exits."

- Risks are skewed toward a hawkish sounding Fed given the recent rates rally, but it would take more than a 2023 median hike to be seen as hawkish; that would likely take Powell signalling concern about financial conditions / inflationary pressures.
- **SEP/Dot Plot:** 2021 GDP and inflation to be revised higher (3.1% for core PCE), 2022 inflation nudged higher – bigger upward revisions would be a hawkish signal.
- No change to 2023 median fed funds dot.
- **Press conference:** Powell to acknowledge "talking about talking about" tapering, but reiterate it will be "some time" before substantial further progress has been made.
- Powell to emphasize that payrolls weakness is due to lack of supply rather than demand, so jobs still on track for substantial progress.
- **Administered rates:** IOER and ON RRP hikes more likely than not.
- **Future action:** BofA sees the FOMC committing to tapering by the Sep 2021 meeting, with implementation in early 2022 and buys wound down to zero by end-2022 (8 meetings, incremental reduction of $10B for Tsys and $5B for MBS per meeting). Rate liftoff in 2H 2023 once core PCE has hit 2% and on track to moderately exceed it; rates to be hiked later but at a faster pace than market pricing.

**CIBC: Too Soon For Formal Taper Warning**

- CIBC sees it as too soon for the FOMC to issue "a formal warning about tapering". However, there might be signals that the Fed was talking about talking about tapering (if only in the minutes).
- **SEP / Dot Plot:** Watch for 1st hike dot median in 2023 (as it won't take many votes to move the needle).

**Citi: Risks Balanced Toward The Hawkish Side**

Citi expects "at least some talking about tapering" at the June meeting, esp with the April minutes and Vice Chair Clarida's associating himself with those minutes.

- While it's still too early to expect a clear signal on "substantial further progress", officials may be ready to admit the economy is making "good progress" and that it "may be becoming time to more fully discuss how a taper should play out".
- Risks relative to market expectations are balanced toward the hawkish side for this meeting. Were Powell to suggest any component is not "transitory"; even a stronger 2021 core PCE projection "may be significant enough to garner market attention".
- **SEP/Dot Plot:** Significant upward revision in 2021 core inflation (mechanically hard to forecast Q4/Q4 core PCE below 2.5%; Citi sees 3+%); 2022 probably nudged higher though still below 2021.
- 2023 median dot to show one hike; hawkish risk of potentially more than one hike.
- **Press conference:** "Powell may perhaps be ready to state in the press conference that the committee discussed tapering in the context of an economy making "good progress" but that "substantial further progress" (the criterion for tapering) is still "some time" away. A hawkish surprise would be if Powell drops the "some time" characterization and instead indicates that tapering is likely in the foreseeable future."
- **Administered rates:** No change to IOER or ON RRP rates.
- **Future action:** September announcement of taper; Dec start; $10B/month Tsys/$5B/month MBS.

**Commerzbank: Tiptoeing To The Exit**

Commerzbank sees the Fed as likely to begin discussing exiting easing measures this week.

- Though employment hasn't made substantial further progress, some on the FOMC want to start a discussion on tapering due to increasing inflation risks (including on the labor supply side). But the data aren't good enough to signal tapering already in the statement.
- **Future action:** Tapering likely to be signalled in Q3 (with lead time before action of about two meetings), with tapering taking place over longer period until late summer 2022. First hike at end-2023.

**Credit Suisse: Hawkish Meeting**

Credit Suisse sees a hawkish meeting: likely Powell will signal the FOMC sees further progress toward its goals and will likely begin to discuss a taper at upcoming meetings; and a hawkish shift in the dot plot.

- **Statement**: Likely to acknowledge strength in economic activity and inflation running above 2%, but no change to fwd guidance.
- **SEP/Dot Plot:** Median hiking dot unchanged for 2021 and 2022, but to move up by 50bps in 2023 to imply two rate hikes. This would take only 3 dots to shift. [Editor's note: it's unclear whether CS is expecting those three shifting dots and others to move to substantially higher than 0.375%, which is what it would take to move the median to 50bps). A few to move to one hike in 2022.
- 2021 GDP and inflation forecast shifted substantially higher; risks for 2022 are for slightly higher estimate (vs 2.0% currently). Unemp could move up slightly in 2021 but 2022/23 likely unchanged.
- **Press conference:** Powell likely to signal taper discussion upcoming; the minutes of this meeting should be particularly interesting.
- **Future action:** Recent strong inflation likely to trigger tapering discussion, "particularly for mortgages, where the market is extraordinarily tight."

**Danske: No Significant New Policy Signals**

Danske does not expect the Fed to send any "significant new policy signals".

- **SEP/Dot Plot:** Median hike in 2023.
- **Future action:** Initial "real discussions" about tapering to begin in September; taper to begin in Jan 2022. First rate hike in Q1 2023.

**Deutsche: Talking About How To Talk About Tapering**

Deutsche expects the highlight of the June FOMC meeting to be "a status check on the Committee's tapering deliberations."

- **Statement:** Little reason for substantive changes; Deutsche also sees an "outside chance" of an announcement on a standing repo facility.
- **SEP/Dot Plot:** Median funds dot unchanged for 2023 hike (in a "close call"). "Ultimately, with the labor market lagging, no strong evidence that the Fed's transitory inflation story is incorrect, and market pricing moving closer to the Fed's views on inflation and the policy rate, the Committee should not yet feel compelled to send a hawkish signal through their rates guidance."
- GDP in 2021 up sharply (6.9%), unemp rate down to 4.4%; core PCE up to 2.9%. Only modest change lower to 2022 growth, 2023 unchanged; unemp and inflation unchanged 2022-23.
- **Press conference:** Powell to indicate that the FOMC discussed what economic conditions they would like to see to begin tapering; Deutsche doesn't anticipate formal thresholds to be provided (in part so optionality is maintained).
- Powell likely to indicate that FOMC believes it will take some time for "substantial further progress"; and that all agreed it was not yet time to taper.
- Powell to repeat bottlenecks narrative on inflation, but "is also likely to note that there is a lot of uncertainty about how long it will take for these bottlenecks to be resolved and for price pressures to moderate".
- **Administered rates:** No change at this meeting; Powell to note that will make as needed in future to ensure that the Funds rate remains within the target range, and in any case would be technical in nature.

**Goldman Sachs: Too Soon To Start The Taper Clock**

While "much has changed since the March and April FOMC meetings", Goldman does not expect the Fed to deliver the first hint at tapering at the June meeting.

- Some FOMC participants have expressed eagerness to begin discussing tapering sooner rather than later, but "we see this as normal disagreement, which was bound to return after a year of consensus around fighting the pandemic, and we think it is still too early for Chair Powell to provide the first hint that would start the taper clock."
- **Statement:** The premise of the language on average inflation targeting is "no longer true": (*"With inflation running 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." ).*

- Fed may make a small fix (change "running persistently to "having run", but at some point FOMC will need to explain what AIT demands if inflation averages more than 2% by the time tapering is complete.
- **SEP/Dot Plot:** No hike in median 2023 dot (but a "close call").
- 2021 GDP and unemployment revised upward (+6.7% and 4.7% respectively), no changes to 2022-23.
- 2021 core PCE up to 2.9%; 2022 and 2023 unchanged. Key question is whether any of the 7 who forecast 1.9% or 2.0% in 2023 in March will raise their forecasts (as they presumably did not show a hike either).
- **Future action:** First taper hint in Aug/Sep, formal announcement in Dec and taper at beginning of 2022.

**HSBC: Tactics Of Tapering**

The FOMC is likely to follow a "middle-of-the-road" approach to tapering at the June meeting, writes HSBC: providing more info to markets on the mechanics of tapering, while emphasizing that no decision on tapering itself has yet been made.

- **SEP/Dot Plot:** GDP growth profile to be broadly unchanged; unemployment too (though some on FOMC may project slower rate of improvement).
- New core PCE forecast around 3.0% end-2012, slowing to around 2.2% in 2022-23
- Median funds rate dot (via slight majority) to shift to a hike in 2023.
- **Press conference:** Powell to say FOMC has begun discussing the potential mechanics of a taper though a decision to begin would remain dependent on "substantial further progress".
- To strive for balanced tone: acknowledging continued economic recovery while stressing future policy decisions depend on actual progress.
- If 2023 median dot shows a hike, Powell to downplay as a major change in FOMC thinking.
- **Administered rates:** IOER and ON RRP could each be raised by 3bp, but Powell would emphasize that these are technical adjustments.
- **Future action:** HSBC expects tapering to begin Dec 2021; rates steady until at least 2023.

**ING: Looking For Hints That Fed Doesn't See Inflation As Transitory**

ING writes of the June FOMC meeting that "markets will be looking for hints on whether the Fed is starting to acknowledge that inflation may not be as transitory as thought" – ING describes their own view as "no-where near as confident as the Fed that inflation will merely be transitory."

- **SEP/ Dot Plot:** Upward revision to 2021 inflation and growth forecast.
- No change in 2023 dot median (one or two officials may raise their dots).
- **Administered rates:** "Close call" on ON RRP adjustment. "But there is a risk that they do it and it changes nothing, in the sense that the reverse repo window remains as popular as ever."
- **Future action:** Fed to fire the starting gun on tapering at Jackson Hole, more formally acknowledged at September FOMC, with announcement at Dec FOMC. First rate hike early 2023, with risks skewed toward earlier action.

**JPMorgan: Rate Liftoff In Late 2023**

JPM sees two questions about tapering: do they talk about it at this meeting, and if they do, how will we learn about it? They expect the FOMC to talk about tapering (given April FOMC minutes flagging "upcoming meetings" for the discussion). And if they do, we may learn about it in Powell's introductory press conference remarks (followed up by restating remains far from "substantial further progress").

- **Statement:** To take the back seat to press conference and dot plot; no changes in guidance, little revision required to economic developments.
- **SEP/Dot Plot:** Median dot to show liftoff in 2023. If so, it's reasonable to see a few more hike dots in 2022.
- GDP and inflation forecasts to be revised higher in 2021, but not as clear that unemp rate will be materially revised. 2023 inflation median unchanged.
- **Press conference:** Powell will indicate that the Committee talked about tapering but that it believes the economy is still far from meeting the "substantial further progress" test to actually begin tapering.
- **Administered rates:** Close call on a change to ON RRP / IOER, but lean toward no adjustment.
- **Future action:** JPM has brought forward their expectations for rate liftoff to late 2023.

- Don’t expect guidance on tapering until a few meetings before it starts (so, the fall).

**Lloyds: Fed May Be Ready To Start Talking About Tapering**

Lloyds says Powell may confirm that discussions on tapering may begin soon.

- The modest change in rhetoric may pave the way for more concrete proposals later in the summer, with the aim of ‘tapering’ beginning around the turn of the year.
- **SEP/Dot Plot:** 2021 inflation will need to be revised up. 2023 dots to show median hike.

**Morgan Stanley: Laying The Groundwork For Increased Flexibility**

Morgan Stanley sees “the balance of recent evidence” as leading them to believe that many FOMC members believe it’s time to provide themselves more flexibility on removing accommodation – and will use the June meeting “to lay the groundwork for increased flexibility by ‘talking about talking about tapering’.”

- **SEP/Dot Plot:** Notable near-term upward revisions to inflation projections.
- Even split on 2023 rate hike median (9 vs 9 dots).
- **Press conference:** “The most likely opportunity for updated guidance on balance sheet discussions to be provided.”
- **Administered rates:** No changes at this meeting.
- **Future action:** Tapering guidance at Sep FOMC, announcement in Mar 2022, start April 2022.

**NatWest: Fed Will Begin To “Talk About Talking About Tapering”**

NatWest expects that at the June FOMC meeting, participants will “begin to opine on when a taper discussion might be appropriate, but emphasize that more progress is needed before [the] taper countdown begins”.

- **Statement:** Only minor changes; most attention will be on the characterization of inflation, with some officials wanting to get ahead of any criticism they are falling behind. Wouldn’t rule out reference to supply-demand mismatches and inflation expectations.
- **SEP/Dot Plot:** Much higher 2021 inflation forecast (2.9%, but only slightly stronger in 2022/23 (2.3%/2.2%). GDP unlikely revised much for 2022-23; gradual labor market improvement in forecasts.
- One hike in 2023. No 2022 hike, but dispersion to rise.
- **Press conference:** If officials do start to talk about discussing a progress-dependent game plan for tapering at the June meeting, Powell could include a line in his prepared remarks that mentions how officials began to talk about talking about discussing a plan for tapering but will emphasize that much more progress is needed before a plan can advance. More likely in Q&A (and likely 1st question).
- **Administered rates:** Both IOER and ON RRP adjusted by 5bps.
- Powell to reiterate the Fed views current inflation as “transitory”.

**Nomura: Getting Closer To Formal Taper Talk**

Nomura sees the June meeting as too early for formal tapering discussions to begin, but expect the FOMC “to forge a consensus that such deliberations will be appropriate relatively soon if economic conditions match expectations”.

- They note: “The April FOMC minutes suggested “a number of” participants viewed it as appropriate to
- begin tapering discussions “at upcoming meetings” if the economy continued to recover strongly. Since April, we think that group has increased to “a majority of” participants.”
- **Statement:** No significant revisions; could downgrade economic conditions due to slow nonfarm payrolls.
- **SEP/Dot Plot:** To show a rate hike in 2023. Higher inflation in 2021, with 2.7% core PCE, though lower (1.8%) in 2022 and unch in 2023. Unch GDP and Unemp forecasts.
- **Press conference:** Powell to emphasize the FOMC remains far from achieving its goals / substantial further progress, and say that tapering discussions did not begin at the June meeting, but may acknowledge that formal taper discussions are likely to start soon.
- **Administered rates:** IOER rate to be hiked, but no change to ON RRP.
- **Future action:** Intensive deliberations on tapering not until July. Nomura now expects tapering to finish over 12 months (previously expected 18), and steeper pace for MBS purchases (ceasing after July 2022). Taper to start in Jan 2022. First hike in Q3 2023.

**Nordea: Bottlenecks, An Early Tapering And Late Hikes**

Nordea expects that the Fed will not be convinced of sustained inflation pressures at the June meeting, but notes that "at the April meeting Powell suggested that inflation would spike but he and the Fed staff underestimated by [how much]".

- **SEP/Dot Plot:** Dots may hint at 2023 hike.
- **Press conference:** Powell is likely to explain most of recent inflation surge away as temporary bottlenecks.
- **Administered rates:** IOER hiked by 5bps; ON RRP counterparty caps widened further.

**Rabobank: Early Warning Signal In A Noisy Environment**

Rabobank sees the Fed as "slowly moving toward tapering its asset purchase program. In order to avoid another taper tantrum Powell has promised us to give early warning. However, the distortions in the current data does not make it easy for the Fed to give clear guidance."

- **SEP/Dot Plot:** Upward revision for inflation in 2021 but should underline pushback against fears that high inflation is permanent in projections for 2022-23.
- The unemp forecast for 2021 may provide a clue about the Fed's numerical threshold for tapering.
- **Administered rates:** Technical adjustment in IOER and ON RRP.
- **Future action:** An early warning signal for tapering in August or September.

**RBC: Would Be Odd If "Talking About Talking About" Taper Doesn't Come Up**

RBC write that "it feels like the initial conversation" around tapering asset purchases is likely to start at this meeting.

- **Statement:** Would be surprising if any material changes.
- **SEP/Dot Plot:** 2023 dot plot seems prime to shift soner rather than later.
- **Press conference:** Powell likely to strike the same cautious tone on the backdrop.

**Scotiabank: 2023 Dot Hike Unlikely Until Powell "Embraces A Taper Dialogue"**

- **SEP/Dot Plot:** 2021 growth might be revised higher, inflation projections up "a touch".
- Unlikely but not impossible that the median dot for a rate hold in 2023 will change. Unlikely that three more members would join the previous 7 anticipating hikes "before Chair Powell embraces a taper dialogue".
- **Press conference:** Powell probably can't simply repeat his answer "no" in response to Q about whether the FOMC is "talking about talking about tapering". Likely to say there are varying opinions across FOMC but "substantial further progress" not yet met.
- **Administered rates:** Change can't be ruled out but not base case.
- **Future action:** Taper discussion to open in Aug or Sep; announced in Dec, to be implemented Jan 2022.

**SEB: Too Early To Signal Tapering**

The June FOMC meeting is too early to signal tapering, writes SEB, who have shifted back their taper timing call.

- **SEP/Dot Plot:** GDP and inflation forecasts likely to rise for 2021, though 2022-23 inflation projections likely largely unchanged. unemp projection of 3.5% by end-2023 likely to remain.
- **Press conference:** Powell's message to be that the Fed does not yet see enough progress to lay out a plan to taper (similar to what he said in April).
- Close call whether median dot shifts higher for 2023.
- **Administered rates:** Likely that Fed hikes IOER and ON RRP rates by 5bp.
- **Future action:** SEB has shifted its call for a tapering decision from September to November (taper itself to begin in December, ending in October 2022), as labor market developments suggest employment is still too low for the Fed to initiate tapering earlier. Powell/FOMC could pave the way at Jackson Hole and / or September FOMC.

**Societe Generale: FOMC To Stir But Are Not Shaken**

SocGen expects communications to begin "on when, how and under what circumstances the Fed could dial back on policy…time has come for at least talking about when and under what conditions – specifically employment and inflation expectations and realized gains."

- **SEP/Dot Plot:** The 2023 rate median is the "nail-biter": SocGen sees a hike as premature for this meeting.
- **Future action:** Fed to announce a tapering program by year-end; beginning in Jan 2022.

**Swedbank: Soon, But Not Yet**

Fed members have started to modify rhetoric on tapering, but official changes will take a little longer, according to Swedbank's June FOMC preview.

- **SEP/Dot Plot:** 2023 dot median likely to stay unchanged.
- Near-term inflation outlook could be revised somewhat higher; no substantial change to unemployment.
- **Future action:** Taper talk more likely to begin at Jackson Hole; taper to start in December.

**TD: Time To Have The Talk**

TD expects a slightly less dovish tone at the June FOMC vs April, with officials starting to talk about a progress-dependent tapering plan while also emphasizing that actual tapering will require much more progress.

- **Statement:** Changes to be minimal.
- **SEP/Dot Plot:** 2021 median core PCE projection sizeably higher but 2022/23 up only slightly, consistent with "transitory" inflation. No big changes to growth or unemployment in 2022-23.
- Median dot to "probably" show a 2023 hike; median to shift to 0.25% (with 9 vs 9).
- **Press conference:** Powell to say the FOMC has started discussing a progress-dependent tapering plan while also emphasizing that action will require much more progress.
- "Perhaps most important will be if and how he modifies the "long way…some time" line he used in opening remarks at each of the last three press conferences. Specifically, at the last press conference he said, "The economy is a long way from our goals and it is likely to take some time for substantial further progress to be achieved."" Powell could replace "some time" with something that puts more emphasis on the data.
- **Administered rates:** IOER and ON RRP on hold for the time being.
- **Future action:** No taper announcement until March 2022. Rate liftoff not until 2024.

**UBS: Taper Discussion Might Start In June**

UBS sees a taper starting in January 2022, but doesn't see a faster/earlier MBS taper (vs Tsys).

- **Press conference:** Powell's comments on the taper to be consistent with the April minutes, saying that the debate has not kicked off but that if the economy continues to make rapid progress, the time to initiate the discussion will probably be in the coming months.
- Part of the discussion on tapering will be around MBS, but UBS does not expect the Fed to taper MBS faster or earlier than Tsys. While multiple FOMC members have suggested MBS purchases should be part of the taper debate, "none has explicitly favored reducing purchases of MBS before those of Treasuries".
- **Future action:** UBS sees a Dec 2021 taper announcement, with discussions ramping up this summer (possibly starting at this meeting). Taper itself to start in Jan 2022 and done over 12 months. Balance sheet reduction to begin 2025, one year after first rate hike.

**Unicredit: Time To Begin Tapering Is Near**

Unicredit thinks the FOMC will "likely indicate that the time to begin discussing a plan for tapering is near" at the June FOMC.

- **SEP/Dot Plot:** Growth / inflation forecasts likely higher for 2021, but inflation in 2023 unlikely to change much (+0.1pp above the 2.1% projected in March).
- One or two more participants see a rate hike in 2023 (ie no median dot increase).
- **Future action:** Base case is tapering discussion formally starts in Aug/Sep, with Dec announcement for 1Q22 taper beginning. First rate hike in late 2023, risks skewed toward an earlier hike.

**Wells Fargo: Opening Taper Discussion**

The opening discussion regarding eventual tapering is likely to take place at the June meeting, according to Wells Fargo.

- **Statement:** Assessment of current state of the economy to be upgraded.
- **SEP/Dot Plot:** GDP and inflation forecasts raised for 2021; 2022/23 inflation projections to show that the Fed still deems recent inflation strength as transitory, and showing risks seen as lying to the upside.
- Median dot could see hike in 2023 (from 11 of 18 officials seeing no hike, to around 9).
- **Press conference:** "Early in the pandemic, Powell said the FOMC was 'not even thinking about thinking about' removing policy accommodation [but Wells Fargo does] not expect that sort of blanket promise at the June meeting."
- **Administered rates:** FOMC "could" raise IOER and ON RRP; would be described as technical.

**Wrightson ICAP: IOER/ON RRP Tweak Is A Close Call**

Wrightson ICAP says "there is no doubt that the FOMC will at least "talk about talking" about a taper in some form" though they surmise "that the minutes … will show that the FOMC did not order up a full set of staff presentations on tapering options this week but left that for a later meeting (probably July). However, a number of FOMC members will raise the topic independently."

- While "if the FOMC were starting from scratch on its balance sheet policies, we doubt there is a single element of today's purchase program that it would choose to retain", Wrightson ICAP doesn't see many options for the Fed at this week's meeting in light of communications objectives.
- **SEP/Dot Plot:** Median dot to show hike in 2023. The communications challenge surrounding such a change "should be manageable".
- Core PCE median almost certainly will move up for 2021, but 2022/23 may not change much. So if an FOMC majority sees a 2023 hike, it's a sign they see stronger employment trends allowing them to begin normalizing, rather than fearing inflation pressures will force them to.
- **Administered rates:** Most likely that Fed announces a "tweak", but could wait until later this month.
- **Future action:** Begin more structured debate about taper in July; settle on framework in September (possibly telegraphed at Jackson Hole), say achieved "substantial" progress in Oct or Dec, taper begins late 2021 or in Jan 2022.

# MNI Policy Team Insights

### MNI STATE OF PLAY: Fed To Stay Patient on QE Taper (Pub. Jun 14, 2021)

*By Jean Yung*

**WASHINGTON (MNI) -** The FOMC this week is expected to cheer steady progress in the Covid-19 recovery but maintain that it will still take some time before the economy meets the Fed's "substantial further progress" bar for tapering asset purchases.

Officials will likely talk about stepping back QE but give no new guidance or refinement of the "substantial further progress" standard. Policymakers have also said the debate over the taper will take several meetings.

The Fed is wary of detailed on-the-record discussions on tapering because such talks have the potential to trigger volatility in financial markets and a tightening effect on the trajectory of the real economy, former officials told MNI.

Chair Jay Powell will likely also downplay any additional projections for liftoff by the end of 2023, former officials told MNI. If two or more policymakers upgrade their forecasts, it is possible the median projection for the Fed's first post-pandemic interest rate hike will move forward into 2023.

With the Fed's emphasis on outcome-based policymaking, the FOMC will need to evaluate the economy's progress against its objectives. Since March, projections for growth and inflation are likely to get a small upgrade, while the outlook for the labor market may be little changed after three months of inconsistent data.

Even with two months of record-setting inflation data, officials are unlikely to have changed their view that the price spikes are transitory and associated with the reopening of the economy. Former officials still saw ample room for medium-term inflation expectations to rise after a decade of downside misses, but they also warned the Fed's perceived indifference to faster inflation may send price expectations lurching higher than policymakers want and force a messy rethink of their stance.

**--JOB MARKET AMBIGUITY**

Payrolls were strong, weak and lukewarm over March, April and May, respectively, creating ambiguity over hiring momentum. On average, the economy added 540,000 jobs a month in the past three months, below the pace that would close the employment gap and see participation recovering substantially by year-end. At the current rate, the labor market is only expected to reach pre-pandemic levels by the end of 2022.

Former policymakers told MNI the Fed won't see enough clear labor market improvement in time to announce tapering of QE at the annual Kansas City Fed Symposium at the end of the summer.

If hiring still doesn't pick up after September, when supplemental job insurance runs out and kids return to school, the road to rebuilding employment might be rockier than previously thought, a Richmond Fed economist told MNI.

**--IOER HIKE**

The Fed is likely to abstain from raising rates paid on reverse repos or excess reserves despite potential financial stability risks stemming from money market funds and as short-term market rates fall.

Former Fed Board division of monetary affairs chief Vincent Reinhart told MNI the Fed could offer money funds relief by raising the rate it pays on reverse repo operations or the rate paid on reserves but the central bank is likely leery of bailing out the industry for the second time in a dozen years. The officials are only likely to move if negotiations over the U.S. debt limit drag on  into the fall, current and former officials told MNI last month.

## MNI: Fed's Powell To Downplay 2023 Liftoff Dots -Ex-Officials (Pub. Jun 11, 2021)

*By Jean Yung and Evan Ryser*

**WASHINGTON (MNI) -** Federal Reserve Chair Jay Powell next week will downplay the significance of additional FOMC members penciling in an earlier rate hike even if the median projection for liftoff shifts forward to 2023, former officials told MNI.

Whether two or more out of 18 FOMC officials bump up their projected liftoff timing -- and move the median forecast -- is a close call, as labor market progress has lagged expectations since March, when the Fed last updated its forecasts, the former officials said.

"There could be some change on the margin, maybe one to two people could accelerate their liftoff timeline, but all things considered I doubt you'll see a big change," former Atlanta Fed President Dennis Lockhart said in an interview.

"Powell may say something to the effect that while indications of the recovery are quite encouraging, the gaps between current data and maximum employment are still substantial, and the committee would like to see further evidence of progress toward its goals."

**--POWELL'S DOT**

Former Richmond Fed President Jeff Lacker told MNI he puts the odds of the median liftoff date floating closer to 2023 at about 40%, adding: "Powell is unlikely to join the move, and would gently try to downplay the significance in the press conference, but he would want to avoid inflaming the debate about which dot is his."

From a public communications perspective, the FOMC "wouldn't even want to show it (liftoff in 2023) in the dot plot until there's some stronger indication of consistent, persistent inflation than what we've seen in the last couple of months," said Tara Sinclair, a former St. Louis Fed economist and member of the Bureau of Labor Statistics technical advisory committee.

Relative to where the economy stood in March, "there are cross-currents" in the data, with growth and inflation above expectations and hiring a bit below, said New York Fed adviser and former Fed Board economist Jonathan Wright. "The majority of the committee will be inclined to put little store on the recent inflation numbers, so I don't think that the 11 participants who expected to still be at the zero lower bound at the end of 2023 will change their minds."

The minority of committee members more worried about inflation expectations are already eyeing liftoff in 2023 or even 2022, he added.

**--EXPECTATIONS REMAIN KEY**

More imminently, weaker-than-expected job growth is likely to push back the timing: https://marketnews.com/mni-feds-jackson-hole-message-muddled-by-jobs of tapering asset purchases, sources told MNI.

"Barring some extraordinary turnaround in the next two jobs reports, I do not see any announcement of tapering being made at Jackson Hole. I would expect it to come later in the year, maybe at the December meeting," Wright said.

Despite two hot inflation reports this spring, "You haven't seen increases in nominal rates and measures of inflation compensation, and trend price measures yet," said Stephen Cecchetti, former New York Fed executive vice president and director of research at the New York Fed. "When the six-month average Trimmed Mean goes up to 2.5%, I'd be worried. But it's below 2%," he said,

Still, Cecchetti conceded that he's "getting nervous," even if he's not outright worried. "There's a lot of nonlinearity in the system," he said, "I'm worried we'll wake up one morning and inflation is not going to be 2%, it's going to be

3%." Fed advisers and ex-staff have warned policymakers' downplaying of faster inflation may send price expectations lurching higher than they want and force a messy rethink of their stance

For now, policymakers are content to sit back and get comfortable with higher inflation expectations and allow the labor market time to re-attain pre-Covid levels of labor participation and unemployment, Lockhart said.

"The Powell Fed is extremely dedicated to completing the job of getting inflation expectations anchored around the target. That strikes me as taking some time to do, and therefore I think starting to hike before 2023 would probably reflect a dilution of that motivation."

## MNI: Jackson Hole Too Early For Powell To Signal Taper (Pub Jun 7, 2021)

*By Pedro Nicolaci da Costa*

**WASHINGTON (MNI) -** Federal Reserve Chairman Jerome Powell might not have enough evidence of a truly robust labor market by this summer's Jackson Hole symposium to deliver the kind of major policy signal of an imminent QE taper Wall Street has come to expect, former Fed economists told MNI.

"There's not going to be any definitive statement made there -- it's an FOMC decision after all," said Charles Steindel, a former long-time New York Fed economist and senior vice president, in an interview. "The most Powell might do at Jackson Hole is give some idea of the criteria for tapering."

Two months of weaker-than-expected job increases are a far cry from the "string" of monthly net job creation numbers near 1 million Powell said he'd like to see before declaring that there has been "substantial further progress" toward the Fed's goals.

"Next week they start the conversation-there are a lot of details to figure out, including how to communicate a taper, when to make the announcement, what to say, what conditions exactly they want to see, how far later to start the actual taper," said Roberto Perli, former Fed board economist. "That will take at least a couple of meetings if not longer."

**--SCARRING FEARS**

The Fed's next meeting is in July and the following one is in September -- after the August Jackson Hole appearance.

"Some vague announcement that if things continue to progress in the right direction a taper could come at coming meetings is possible at Jackson Hole or the September meeting. But they sure don't seem to be in a great hurry, and the data give them cover," Perli said.

After March's payrolls rise was initially reported at 916,000 new jobs, markets built in the expectation that similar gains would follow in subsequent months, allowing the Fed to signal a taper in the summer and to actually begin reducing bond buys by late 2021 or early 2022.

Since then, not only was March's gain revised down to 785,000, employment growth slowed sharply to just 285,000 in April before up in May, but only to 559,000.

The data have raised new concerns about possible longer-term effects from the shutdowns on the labor market that could lead to the kind of scarring that worries policymakers.

That means Fed officials will need more time to distinguish signal from noise in the job market data in the same way that they are having to decipher how much of the recent spike in inflation: https://marketnews.com/mni-fed-to-bend-guidance-toward-faster-taper-ex-official s is transitory and how much of it might prove a more permanent phenomenon.

**--MBS TAPER**

"I think the Fed is probably willing to wait until the unemployment insurance supplement ends and schools restart to make judgments on the labor market," Joseph Gagnon, a former Fed board economist, told MNI.

Neither will happen until September, making it less likely that Powell will want to deliver any robust signals during his late August remarks at the Wyoming mountain lodge.

Danielle DiMartino Booth, a former adviser to the Dallas Fed, told MNI she believes the Fed may begin to lay the groundwork for a QE taper that's led by mortgage-backed securities given the strength, something MNI has reported Fed officials are actively considering.

"Splitting off MBS tapering from that of Treasuries could be an elegant and politically palatable compromise -- move away from mortgages but keep the Treasury QE running at full throttle until much more progress is made on the employment front," she told MNI.

St. Louis Fed President James Bullard recently told MNI in an interview he thought expectations for gangbuster employment gains in the spring were premature given lingering worries about the pandemic and issues surrounding childcare.

Richmond Fed economist Thomas Lubik told MNI last week that post-Covid structural challenges including mismatches between available jobs and workers could prolong the labor market recovery.

## MNI: Fed To Consider MBS-Led Taper As Housing Booms

*(**Pub. May 20, 2021**)*

*By Pedro Nicolaci da Costa and Evan Ryser*

A surging U.S. housing sector is forcing Federal Reserve officials to consider a policy option many FOMC members would likely prefer to avoid, current and former officials tell MNI -- the possibility of leading a taper of QE with a larger reduction of mortgage bonds than Treasuries.

"I think there'll be an appetite for tapering MBS a bit faster than Treasuries," said Jonathan Wright, a former member of the Fed Board's division of monetary affairs and current New York Fed adviser.

"There are those who are more worried and would particularly want to dial back on MBS and I could actually see that being a consensus of the Committee, that they want to first of all get out to the MBS market."

U.S. home prices jumped 12% in February, matching a record increase in February 2006, just before the housing market cratered and dragged the economy into the Great Recession. Housing starts for April also hit a 15-year high.

"The Fed has to start the tapering process one way or another and MBS is a good category to start with given the strength in housing," said Chan-Guk Huh, a former San Francisco Fed economist.

When the Fed first embarked on QE in response to the Great Recession, it bought mortgage-backed securities because the housing market was the focal point of the crisis. Officials then argued they were trying support the broader economy, not a specific sector, a view Fed Chair Jerome Powell reiterated in his last press conference.

But minutes from the Fed's April meeting showed "a number of participants commented on valuation pressures being somewhat elevated in the housing market."

**--THIS TIME IT'S DIFFERENT**

While there is broad consensus today's housing market is not as susceptible to a crisis thanks to Dodd-Frank and other reforms which have strengthened banks and boosted their capital, there are still signs of froth, and many first-time homebuyers are being priced out of the market.

"Households have plenty of equity, and the credit quality of the stock of mortgage debt is much higher than in 2006 -- there's no subprime to speak of," said Andrew Haughwout, senior vice president at the New York Fed who focuses on the housing sector. But he pointed to growing investor activity in the market. "It's not nearly as high a share as back in 2006. But it's growing and it's something we need to watch."

That kind of shift has already prompted a couple of regional Fed presidents to publicly express openness toward the idea of leading a taper with MBS.

**--A VOCAL MINORITY**

The Fed is currently buying USD120 billion in bonds monthly -- USD80 billion in Treasuries and USD40 billion in MBS -- to support the economy, and has vowed to keep doing so until the country makes "substantial further progress" toward stable price and full employment goals.

"I think this would be a good topic for debate and will be debated once that topic is open but let's let the chair open up that discussion," Bullard told reporters during a Wednesday press briefing in response to a question from MNI, sketching out the broad lines of a disagreement among policymakers over how to treat MBS and Treasuries.

"Some people would say they are very similar because Freddie Mae and Freddie Mac are still in conservatorship so it's like a Treasury bond," he said. "Other people think there's more segmentation in the market and you're feeding into the housing boom by purchasing the MBS."

Eric Rosengren and Robert Kaplan, presidents of the Boston and Dallas Feds respectively, appear to be in the latter camp.

"I do think that as we think about tapering one of the things that we are going to have to think about is at what speed we taper the Treasuries versus the mortgage-backed securities," said Rosengren in a recent Q&A. "One of my financial stability concerns would be if the housing market gets too overheated."

The Fed has historically been reluctant to either acknowledge or try to prick asset bubbles, and remains that way today.

## MNI: Fed IOER Hike On Hold Unless Debt Limit Talks Drag On

*(**Pub. May 21, 2021**)*

*By Evan Ryser*

Possible hikes in the Federal Reserve's rates on overnight reverse repos and excess bank reserves look to have been parked for now, with officials only likely to move if negotiations over the U.S. debt limit drag on into the fall, current and former officials told MNI.

A shift in the Treasury's financing plans earlier this month will likely result in its releasing fewer reserves into the banking system. That combined with a recently-upsized overnight reverse repo facility is alleviating downward pressure on the benchmark fed funds rate and paring back expectations for an IOER and ON RRP hike in the near term.

"The fact that the Treasury is not going to be holding [reserves] down even more means it's got to help at the margin and help prop rates up a little bit," said Todd Keister, a former New York Fed economist currently a visiting scholar at the Philadelphia Fed.

However, the longer the debt ceiling talks drag on, the more Treasury's cash balance would fall, renewing pressure on the fed funds rate. Treasury said May 3 it will target a July 31 cash balance of USD450 billion, more than USD300 billion higher than previous estimates, and slow its T-bills paydowns by USD150 billion.

**--DEBT CEILING UNCERTAINTY**

Lawmakers are sharply divided on the debt limit, with Republicans writing into caucus rules they will not support raising the ceiling without spending cuts. While Secretary Janet Yellen has said the Treasury's "extraordinary measures" to make payments on previous debts could run out in the early summer in some scenarios, some analysts say Treasury's cash balance could provide a cushion into October.

If the squabble goes on long enough, the Treasury could need to ramp up bill issuance more rapidly after the debt limit is dealt with, which could lift short-term rates again, sources said. Fed research shows an additional trillion dollars of Treasuries with less than a year to maturity tends to increase fed funds by about 3bps, MNI previously reported

"At some point the downward pressure would become upward pressure, but that is hard to know precisely and hard to establish," Antoine Martin of the New York Fed told MNI.

Some outside analysts warn of a small chance the Fed could surprise with a pre-emptive move on its administered rates as soon as the June meeting. But sources told MNI the Fed prefers to be patient.

Even as money market rates have dipped into negative territory, with some T-bill rates this week at 0%, the New York Fed has signaled there's little reason to increase administered rates without additional "undue downward pressure" on the benchmark fed funds rate. The NY Fed's markets chief Lorie Logan has said that some negative rates, particularly the SOFR first percentile, appear "technical in nature."

**--RELIEF VALVE**

"We are now in a situation where it's kind of convenient for the Fed to keep targeting the fed funds rates because that rate seems to be more stable and doesn't move much whenever the repo rates go down," said Quentin Vandeweyer, who worked in the Research Directorate of the European Central Bank and is an outside Fed adviser.

He added he expects short-term rates to remain "more or less stable around where they are right now, especially because of the reverse repo facility that's in place and that's absorbing some of the movements in rates."

The central bank appears to be satisfied with increased usage of the reverse repo facility after per-counterparty caps were lifted in mid-March to USD80 billion from USD30 billion. Usage has rocketed to over USD350 billion in the past two months, and some ex-officials expect that could temporarily spike to USD1 trillion at quarter-end next month, well above the previous all-time high of roughly USD650 billion.

"The Fed appears much more comfortable with the reverse repo facility than it did in 2013 and 2014 when it was started," said Keister, the Philly Fed visiting scholar. "Maybe it could get much bigger going forward and the most likely outcome would be that would be just fine."

## MNI INTERVIEW: Fed's Bullard Mindful of Inflation Expectations (Pub May 17, 2021)

*By Pedro Nicolaci da Costa*

**(MNI) -** St. Louis Fed President James Bullard told MNI in an interview Monday that rising inflation expectations are so far consistent with a shift in the Federal Reserve's goal of making up for past undershoots of its 2% inflation target, and market-based measures bear watching for signs of any worrisome spike.

Bullard isn't too concerned about April's 4.2% inflation rate, and instead is monitoring market measures like the spread between nominal Treasuries and inflation-backed bonds.

"We were certainly expecting year-over-year comparisons to make the inflation number look hot -- that certainly happened," Bullard told MNI. "I don't think that those are the kinds of lasting increases of prices that you would call inflation, but I do think it's enough to have sent inflation expectations somewhat higher."

The rise in TIPS-based inflation break-evens to around 2.7% on a CPI basis is "suggests the committee will be able to move inflation somewhat above target for some time which is what the new framework is aiming for," he said.

**PATIENCE ON TAPERING**

Asked about his tolerance for higher inflation expectations, Bullard said break-evens at 2.75% for the CPI would be consistent with a reading of around 2.45% for the Fed's preferred PCE inflation gauge -- and thus his desired degree of overshoot. Bullard said he's also comforted by five-year forward contracts showing inflation ebbing in the latter portion of the coming ten-year period.

"Could it go higher? Absolutely. That's something I would want to look at and think about," he said. "If you had some expectation where let's say the five-year (TIPS breakeven) were considerably higher than it is today and then five-year/five-year forward was even higher than that, that would suggest a de-anchoring of inflation expectations and in that circumstance I think the committee would have to get more active in trying to reassure markets."

Bullard said he could raise his March forecast for 6.5% growth this year, though he hasn't formally gone back to revise that or his view inflation will register around 2.5%. "I'd now be willing to move that up somewhat," he said of his growth call. Even with growth that Bullard thinks will be around an annualized 10% this quarter, he pushed back against talk from investors and former policymakers about a near-term tightening of monetary policy.

**JOBS MOMENTUM**

"I would like to see a more definitive end to the pandemic before we change monetary policy," Bullard said. "The probabilities are rising probably to pretty high levels that it will come to an end. But you'd really like it to be more definitively finished than it is today and then at that point we can open up discussions as to where to go next."

"It's important for Jay to open that discussion as opposed to members of the committee," he said, referring to Fed Chair Jerome Powell.

The Fed is currently buying USD120 billion a month of Treasury and mortgage bonds in order to support the economic recovery. The central bank has said it needs to see "substantial further progress" toward its stable price and full employment goals before officials begin reducing the pace of QE. Bullard said he wasn't surprised by an April jobs report showing a net gain of just 266,000 new jobs, because the momentum should build more towards the end of the year.

**SEEKING TIGHTER JOB MARKET**

"April was a little bit too early to expect really big jobs numbers," he said. "You still have children at home in a lot of school districts in various states of flux. As of April, you still had a lot of people very nervous about the pandemic itself."

"Labor markets are tight. If you look at the unemployment-to-vacancies ratio it's one of the lowest readings we've seen and approaching the lows of the previous expansion," Bullard said.

Fed advisers have told MNI they see the prospect that April's jobs disappointment may not have been a one-off, because they believe labor market matching issues will lengthen the reversal of Covid-linked layoffs.

"We've made a lot of progress so far and with this booming economy I think we're likely to move even further in the direction of a tight labor market," Bullard said.