Patient Fed Shrugs off Possibility of Overheating

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The conclusion of the two-day FOMC meeting revealed *no change in monetary policy*, and a resolute Fed inclined to hold rates steady as the economy rapidly improves and the labor market moves back toward full employment.

The updated inflation forecast indicated Fed officials believe price pressures will rise briefly this year before retreating. The Personal Consumption Expenditures (PCE) index, the Fed's preferred measure, is forecasted to climb from +1.5% to +2.4% in 2021, before declining to +2.0% in 2022 and +2.1% in 2023. Since committee members have indicated a willingness to allow inflation to move above their +2.0% target "for a time" before reining it in, the updated forecast continues to support a patient Fed.

The new "dot plot" (which was probably the most anticipated piece of information coming from today's meeting) showed committee members on the whole, expect to maintain the overnight target rate at 0.00% to 0.25% *through 2023*. It's worth noting that four of 18 Fed officials expect at least one rate increase next year, while seven expect at least one increase in 2023, up from five. *This leaves 11 of 18 expecting no increase before 2024.*

The committee sees +6.5% GDP growth for 2021 (up from +4.2% at the previous meeting) with the unemployment rate tumbling to 4.5% by year-end, *within a single percentage point of the pre-pandemic, five-decade low*. Although the Fed did not announce an increase on its *Interest on Excess Reserves* (IOER) rate, it did raise the daily limit on reverse repo operations from $30 billion to $80 billion, which is expected to have a similar effect to an IOER increase.

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In his prepared statement at the post-meeting press conference, Fed Chair Powell said:

- Some of the worst outcomes may have been avoided, although no one should be complacent.
- The economy is still a long way from our inflation and employment goals.
- The recovery has been uneven.
- Headline unemployment is actually much higher due to the decline in the labor force.
- The Fed is committed to using its full range of tools.

In the Q&A period, Powell said:

- The outlook has improved very significantly since the last meeting.
- The committee is looking for substantial further progress; actual, not forecasted progress before beginning to taper QE asset purchases.
- The committee will not act pre-emptively based on just forecasts.
- The Fed will provide as much advance notice as possible when the time comes.
- The stance of monetary policy remains appropriate.
- Committee forecasts remain extremely uncertain.

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Powell chose not to respond to a question on an "operation twist" type program, and when asked about the SLR exemption for banks set to expire in two weeks, Powell promised an announcement *in the coming days*.

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The market reaction was relief. The DOW climbed more than 150 points after learning the Fed's intent to remain patient, while the Nasdaq reversed a small loss and climbed into positive territory on the day. Both the DOW and S&P500 are now at fresh record highs. Bonds are mixed on the day, with a rally on the short-to-intermediate end of the curve and a selloff on the long end…although the Fed's assurance has pushed bond prices well off their lows for the day.

Market Indications as of 3:10 P.M. Central Time

DOW	UP 189 to 33,015 (NEW HIGH)
NASDAQ	UP 54 to 13,525 (HIGH: 14,095)
S&P 500	UP 11 to 3,974 (NEW HIGH)
1-Yr T-bill	current yield 0.06%; opening yield 0.07%
2-Yr T-note	current yield 0.14%; opening yield 0.15%
5-Yr T-note	current yield 0.80%; opening yield 0.83%
10-Yr T-note	current yield 1.64%; opening yield 1.62%
30-Yr T-bond	current yield 2.42%; opening yield 2.38%