Markets Sigh as the Fed Indicates No Change for Now

Scott McIntyre, CFA
HilltopSecurities Asset Management
Senior Portfolio Manager
Managing Director
512.481.2009
scott.mcintyre@hilltopsecurities.com

Greg Warner, CTP
HilltopSecurities Asset Management
Senior Portfolio Manager
Director
512.481.2012
greg.warner@hilltopsecurities.com

This afternoon, Fed officials voted unanimously to hold interest rates steady. In the official statement released at the conclusion of the July FOMC meeting, committee members acknowledged the U.S. economy has made progress toward meeting the goals necessary to taper asset purchases, but will continue to monitor that progress. Since the Fed has been adamant it will give ample notice before tightening policy, it's now less likely that tapering will be announced at the next FOMC meeting in September. For now, the $120 billion in monthly QE asset purchases will continue.

Comparing the previous statement to today's shows Fed officials are no longer seeing a reduced covid spread, and reiterated that the path of the economy will depend on the course of the virus.

The statement's inflation assessment remained as written: "Inflation has risen, largely reflecting transitory factors." *Chairman Powell didn't sound quite as sure about this in the post-meeting press conference.*

After considerable discussion at the previous meeting, the committee announced two permanent standing repo facilities, one for Primary Dealers and other financial institutions, and another for foreign institutions. These liquidity backstops will add stability to the markets, but will not directly affect yields.

In the press conference that followed, Fed Chairman Powell took a more dovish overall stance than the statement. He cautioned that the headline unemployment rate understates the labor market weakness, indicating (once again) that "further progress is needed." Powell repeated that the Fed seeks a return to "full employment" and there is "still a long way to go" on this front.

The statement's inflation assessment remained as written: "Inflation has risen, largely reflecting transitory factors." Chairman Powell didn't sound quite as sure about this in the post-meeting press conference.

In his prepared remarks, Powell said that household spending was rising "at an especially raid pace." In the Q&A that followed, Powell said it was plausible the Delta virus surge could cause a pullback in consumer behavior later this year.

The Chairman said that although inflation is expected to move toward the Fed's +2.0% target over time, there is a possibility that inflation could be higher and more persistent than expected. In the near-term, Powell said inflation risks are to the upside. In the medium term, Powell expects inflation will move lower. Powell continues to walk a fine line between dismissing price pressure as temporary, and admitting that there are upside risks that will be carefully watched.

On tightening policy, Powell reiterated that the committee was nowhere near raising interest rates "…not even thinking about it." The phrase "substantial further progress" came up several times. *This seems to be the key to the policy timing, although it's far from clear what this progress would look like.*

On tightening policy, Powell reiterated that the committee was nowhere near raising interest rates "…not even thinking about it."

The bond market has rallied, while the equity markets have generally improved since the announcement. The bottom line seems to be that the Fed isn't any closer to tightening, and in the midst of another virus surge (albeit isolated), uncertainty has increased. For now, the Fed will continue to monitor the virus, the uneven labor market recovery and inflation. The next major Fed event and the next possibility of a shift in monetary policy will take place next month in Jackson Hole, Wyoming.

For now, the Fed will continue to monitor the virus, the uneven labor market recovery and inflation.

Market Indications as of 3:18 P.M. Central Time

DOW	Down 128 to 34,931 (HIGH: 35,144)
NASDAQ	Up 102 to 14,763 (HIGH: 14,841)
S&P 500	Down 1 to 4,401 (HIGH: 4,422)
1-Yr T-bill	current yield 0.07%; opening yield 0.06%
2-Yr T-note	current yield 0.20%; opening yield 0.20%
3-Yr T-note	current yield 0.36%; opening yield 0.36%
5-Yr T-note	current yield 0.70%; opening yield 0.71%
10-Yr T-note	current yield 1.23%; opening yield 1.24%
30-Yr T-bond	current yield 1.88%; opening yield 1.89%