A Hawkish Skip

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

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

Financial markets have spent the last several weeks gravitating toward the idea that the FOMC would not raise the fed funds target for an eleventh straight time at today's meeting. Prodded along by a few tentative signs of easing inflationary pressures, uncertainty about the implications of March's banking turmoil, and knowledge that the 500 basis points of rate increases implemented thus far are still working their way through the system, markets had concluded the FOMC would take a pause. To some, the word *pause* signaled the Fed may not hike again, to others it meant that the Fed would skip hiking at this meeting, only to hike again at a future meeting.

This afternoon, the FOMC leaned in with what could best be described as a hawkish skip. While they left rates unchanged today, the new summary of economic projections, the so-called dot plot, conveyed a much more hawkish note than markets had anticipated. The forecast called for another 50 basis points of rate hikes before the year is over with a median estimate of 5.625%, versus the 5.125% from March's forecast. In addition, the median estimate for the end of 2024 rose by 25 basis points to 4.625%. It's likely this hawkish forecast reflects a desire to keep the markets from reading too much into the pause and thereby easing financial conditions prematurely.

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During his opening remarks at the post meeting press conference, Chair Powell noted that core inflation readings remain well above the Fed's target and that the process of getting inflation back to the 2% target "has a long way to go." In response to a question, Powell acknowledged they have "not seen a lot of progress" on core inflation and that "we want to see it moving down decisively." Powell also noted that, "Nearly all committee participants expected it will be appropriate to raise interest rates somewhat further by the end of the year." Indeed, the dot plot shows 12 of the 18 members forecast another 50 bps of hikes, four signal 25 bps more, and only two members think the Fed is done.

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The initial reaction from financial markets was quite negative, with stocks lower and yields higher. The 2-year Treasury note went from a yield of 4.63% just before the announcement to 4.80% in the minutes immediately following its release. The 2-year has since traded back down below 4.70%. Likewise, equities sold off on the announcement but have since clawed back much of the lost ground.

At this early stage, it appears the Fed has managed to do exactly what it had hoped to. They've bought themselves time to monitor incoming data and to assess conditions without leading markets to ease financial conditions. Whether or not the Fed hikes again will be dictated by the path of core inflation. Despite a steep decline in the headline CPI reading from last summer's peak of 9.1% to 4% last month, core-CPI was 5.3% in May, while core-PCE was well more than double the Fed's target at 4.7% in April. If those figures don't move "down decisively" in the months ahead, we can expect additional hikes to come.

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Please see disclosure starting on page 2

Market Indications as of 2:42 P.M. Central Time

DOW	Down -253 to 33,959 (HIGH: 36,800)
NASDAQ	Up 20 to 13,593 (HIGH: 16,057)
S&P 500	Up 7 to 4,376 (HIGH: 4,797)
1-Yr T-bill	current yield 5.27%; opening yield 5.21%
2-Yr T-note	current yield 4.73%; opening yield 4.67%
3-Yr T-note	current yield 4.35%; opening yield 4.29%
5-Yr T-note	current yield 4.03%; opening yield 4.00%
10-Yr T-note	current yield 3.81%; opening yield 3.82%
30-Yr T-bond	current yield 3.88%; opening yield 3.92%