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# Markets Roar as the Fed Teases Rate Cuts

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As widely expected, Fed officials voted unanimously today to hold the overnight funds rate steady in a range of 5.25% to 5.50% for the third straight meeting, but it was a shift in the FOMC outlook and dovish comments by Chairman Powell that fueled a massive post-meeting rally in both stocks and bonds.

The new "dot plot" showed rate cuts totaling 75 basis points for 2024, bringing the end-of-year midpoint down to 4.625%. By comparison, the previous dot plot from the September meeting had indicated a year-end overnight target of 5.125%. The new rate projection was widely dispersed with six committee members at the median, eight expecting fewer cuts and five expecting more. By the end of 2025, the dot plot indicates the overnight target will be another 100 bps lower with a midpoint of 3.625%, and by the end of 2026, 2.875%.

The December summary of economic projections (SEP) was more favorable across the board. GDP for all of 2023 is now expected to be +2.5% to +2.7%, up from +1.8% to +2.6% in September. The GDP forecast for 2024 was lifted slightly to a range of +0.8% to 2.5%. *Note: no recession expected.*

On the inflation side, the committee's new core PCE forecast for 2023 is +3.2% to +3.7%, down from +3.5% to 4.2% in September. This indicates Fed officials believe monetary policy has proven more successful than previously expected in lowering inflation. FOMC members foresee a soft landing with inflation retreating while the economy continues to grow, albeit at a slower pace.

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The Official Statement released at the conclusion of the meeting was viewed as quite dovish, although the side-by-side comparison reveals very few changes. The new statement continued to describe inflation as "elevated," but added that it had "eased over the past year." Whereas the November statement said the economy had expanded at a strong pace in the third quarter, today's update noted more recent growth had slowed.

Oddly enough, within the committee's brief assessment of monetary policy, analysts seem to have honed-in on a single added word. The previous statement had talked about *the extent of additional policy firming that may be appropriate*, while the new statement talked about the extent of "any" additional firming that may be appropriate. It's subtle, but it seems to imply the committee now believes the next move will be a rate cut.

In the press conference that followed, Powell led off (as he has all year) by saying inflation remains too high. He then added another tried-and-true catchphrase in saying "the committee is proceeding carefully." This doesn't indicate Fed officials are as convinced as the markets that a rate cut is in play for March. In fact, the Fed Chairman said the committee was prepared to tighten further if needed and has not taken rate hikes off the table. Just minutes later, Powell acknowledged committee members had discussed rate cuts at the meeting, in particular *the timing of rate cuts*. This admission is a first for the cycle, and is probably the most dovish revelation of the afternoon.

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Powell must of have realized someone would ask about the added word in the Official Statement, so he addressed it head-on, saying "any" was an acknowledgement that policy was at or near its cycle peak. He also mentioned it was premature to declare victory, although by this point the markets weren't paying attention to feeble balancing efforts.

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Powell, surprisingly, offered up *even more* dovish comments in the Q&A session, noting welcomed progress on inflation and saying that rate hikes were no longer the base case for the committee.

This afternoon's rally has pushed bond yields to the lowest point since early summer along most of the curve. The futures market has now priced-in nearly 150 bps of rate cuts for 2024 with the first likely at the March FOMC meeting. All of the major stock indexes are up significantly as equity investors embrace the upcoming promise of lower rates.

## Market Indications as of 3:23 P.M. Central Time

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| DOW | Up 512 to 37,090 (NEW HIGH) |
| NASDAQ | Up 201 to 14,734 (HIGH: 15,871) |
| S&P 500 | Up 63 to 4,707 (HIGH: 4,797) |
| 1-Yr T-bill | current yield 4.92%; opening yield 5.11% |
| 2-Yr T-note | current yield 4.44%; opening yield 4.73% |
| 3-Yr T-note | current yield 4.16%; opening yield 4.42% |
| 5-Yr T-note | current yield 3.98%; opening yield 4.22% |
| 10-Yr T-note | current yield 4.03%; opening yield 4.20% |
| 30-Yr T-bond | current yield 4.18%; opening yield 4.30% |