

Markets Rally on Powell's Confidence

As expected, Fed officials voted unanimously this afternoon to hold the overnight rate steady for the sixth consecutive meeting. The official statement, released at the conclusion of the meeting, added "In recent months, there has been a lack of further progress toward the committee's 2% inflation objective." The notion that the Fed sees inflation progress stalling is an important takeaway, *although hardly a surprise*.

The remainder of the canned statement reiterated key points, in particular, "the committee does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2%." This continues to indicate the next move will be a rate cut, which probably eased more than a few minds. Powell implied this same point in his post-meeting press conference.

Another important outcome of this meeting is that Fed officials will begin slowing the quantitative tightening pace beginning on June 1st. The monthly balance sheet runoff of Treasury securities will decrease from a maximum of \$60 billion to \$25 billion, while the monthly pace of MBS runoff will continue at \$35 billion. The simple fact that the bond market will be absorbing less supply beginning next month is positive and has contributed to a broad rally in both stocks and bonds.

At the post-meeting press conference, Chairman Powell began with balanced, mostly paint-by-numbers opening remarks that mirrored the committee's official statement. Powell said (once again) the committee remains highly attentive to inflation risks, and gaining the confidence to cut rates is likely to take longer than previously expected. He went on to say Fed officials will continue to make decisions on a meeting-by-meeting basis.

Powell reported any MBS runoff exceeding \$35 billion per month will be invested in Treasuries. This makes the QT announcement a bit more dovish for the Treasury market.

In the Q&A that followed, when asked if Fed policy was *sufficiently restrictive*, Powell responded that he considers current policy to be *restrictive* and cited evidence that policy is already weighing on demand. Over time, Powell believes policy will be *sufficiently restrictive*. This implies (again) that the committee is not considering a rate hike, but will maintain restrictive policy for as long as needed.

Most questions this afternoon were focused squarely on the path of monetary policy. Reporters hoped to pin Powell down on the timing of the next move, but Powell's consistent response was that future data will dictate future policy. One important admission was that conditions have already grown more restrictive as market yields are higher than when the year began, which is appropriate given the uptick in inflation. *In other words, the market has already tightened policy.*

Investors were concerned that Powell would strike a hawkish tone this afternoon, but he remained steadfast in his position that, over time, the FOMC will achieve its inflation objective.

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
Managing Director
512.481.2012
greg.warner@hilltopsecurities.com

The notion that the Fed sees inflation progress stalling is an important takeaway, although hardly a surprise.

The simple fact that the bond market will be absorbing less supply beginning next month is positive and has contributed to a broad rally in both stocks and bonds.

Market Indications as of 2:37 P.M. Central Time

DOW	Up 321 to 38,136 (HIGH: 39,807)
NASDAQ	Up 112 to 15,770 (HIGH: 16,442)
S&P 500	Up 40 to 5,075 (HIGH: 5,254)
1-Yr T-bill	current yield 5.20%; opening yield 5.21%
2-Yr T-note	current yield 4.95%; opening yield 5.03%
3-Yr T-note	current yield 4.80%; opening yield 4.87%
5-Yr T-note	current yield 4.65%; opening yield 4.72%
10-Yr T-note	current yield 4.63%; opening yield 4.68%
30-Yr T-bond	current yield 4.75%; opening yield 4.78%

The paper/commentary was prepared by Hilltop Securities Asset Management (HSAM). It is intended for informational purposes only and does not constitute legal or investment advice, nor is it an offer or a solicitation of an offer to buy or sell any investment or other specific product. Information provided in this paper was obtained from sources that are believed to be reliable; however, it is not guaranteed to be correct, complete, or current, and is not intended to imply or establish standards of care applicable to any attorney or advisor in any particular circumstances. The statements within constitute the views of HTS and/or HSAM as of the date of the document and may differ from the views of other divisions/departments of affiliates Hilltop Securities Inc. In addition, the views are subject to change without notice. This paper represents historical information only and is not an indication of future performance. Sources available upon request.

Hilltop Securities Asset Management is an SEC-registered investment advisor. Hilltop Securities Inc. is a registered broker-dealer, registered investment adviser and municipal advisor firm that does not provide tax or legal advice. HTS and HSAM are wholly owned subsidiaries of Hilltop Holdings, Inc. (NYSE: HTH) located at 717 N. Harwood St., Suite 3400, Dallas, Texas 75201, (214) 859-1800, 833-4HILLTOP.