Fed Unfiltered

WEEKLY REPORT 9/27/22

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- *Bullard – Unemployment to go higher.*
- *Recession – What do the indicators say?*
- *Inflation – A rollercoaster ride is expected.*

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Bullard – No Need to Relive the 1970's

- "These levels of inflation are similar to levels that you would have seen in the 1970s or early 1980s, so this is something we have not experienced since the days of Paul Volker. And the problem with the 70's was not just that there was a tolerance for high inflation, but hat the inflation was volatile and the real economy was also volatile with four recessions in 13 years culminating in the 1982 recession, which sent unemployment all the way to 10.8% in the U.S. at the peak. So this is a serious problem and we need to be sure that we respond to it appropriately and not replay the very volatile era of the 1970s."
- "On the labor side of our mandate, we're doing very well. The unemployment rate in the U.S. is 3.7% … Even is inflation was at 2% and you had ordinary monetary policy going on, you would still expect the unemployment rate to return to its natural level (approximately 4.4%) and that would be higher than what it is today."
  Source: James Bullard, Speech: Barclays-CEPR International Monetary Policy Forum, 9/27/22

FOMC – Out in Force

- Over the last three days, 10 of the 17 Fed Governers or Presidents were either interviewed, gave a speech or published an essay.
- The messaging is fairly similar: rate hikes will continue (possibly to 4.50%) and will remain at a restrictive level (above 2.50%) until there is clear evidence of inflation declining (several months in a row). The committee has no interest in the stop and go (rate hikes/rate cuts) approach of the 70's.
- Despite the effort, the 2yr moved up only 10bps in 2-days and is down 17bps in early trading on Wed.

Recession – What do the Indicators Say?

- "In the two quarters leading up to the average recession, all measures were still experiencing varying degrees of positive growth. Real personal income grew at an average of 0.62% prior to the average recession, while industrial production grew slightly, by 0.05%. Meanwhile, immediately following the onset of the average recession, all six indicators declined, which ultimately persisted for the entirety of the recession. Interestingly, the last column in the table shows the most recent quarter (2020:Q2) of each indicator. All except wholesale-retail sales (which was barely negative) were still experiencing positive growth following the first quarter of 2022."
- "Given the fact that the majority of the indicators are still experiencing growth rather than decline, there may not yet be a strong argument supporting the assertion that there currently exists a significant and widespread decline in economic activity. While the job of identifying the dates of peaks and troughs belongs to the NBER BCDC, it does face a number of challenges in doing so, and historically the committee tends to announce its decisions after the fact. However, we can know for certain that careful consideration will be given to several broad measures of economic activity outside of GDP growth."

Indicator	Prior to Recession	Two Subsequent Quarters	Entire Recession	Most Recent Quarter (2022:Q2)
Real personal income	0.62%	-0.83%	-1.52%	0.24%
Nonfarm payroll	0.30%	-1.32%	-2.51%	0.84%
Household employment	0.30%	-1.42%	-1.87%	0.27%
Real personal consumption	0.48%	-2.92%	-3.72%	0.26%
Wholesale-retail sales	0.28%	-0.95%	-3.54%	-0.09%
Industrial production	0.05%	-2.79%	-5.88%	1.49%

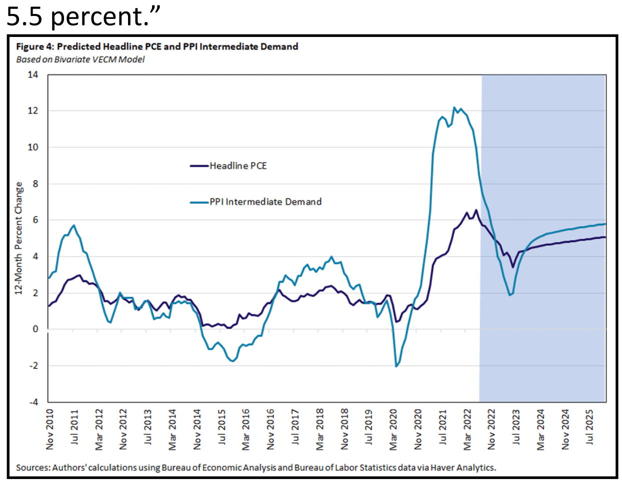
SOURCES: FRED (Federal Reserve Economic Data) and authors' calculations.

NOTES: Data on real personal consumption only go as far back as 2002. Therefore, the fact that the indicator faces the sharpest decline may be, in some part, due to a limited number of observations. Additionally, data are available for the second quarter of 2022 for all indicators except wholesale-retail sales, for which the most recent data only go as far as the first quarter of 2022.

Source: St. Louis Fed, Report: Is the U.S. in a Recession? What Key Economic Indicators Say, 9/26/22

Inflation – We Could See Sub 2.0% Within 12-months

- "What do the latest PPI and PCE readings imply for inflation next year? We can use our simple model to forecast inflation, shown in Figure 4."
- "Assuming no further shocks to consumer or producer prices in the future, the model suggests PPI inflation will fall below 2 percent in the second quarter of 2023, due to high base effects from elevated inflation in spring 2022. However, after those base effects roll off the calculation, PPI inflation is projected to rise further, ending 2024 at 5.5 percent."



Source: Richmond Fed, Report: Building a Pipeline Between Producer and Consumer Prices, 9/23/22

"Quote of the Week
"In the book of life, the answers aren't in the back."
--- Charlie Brown

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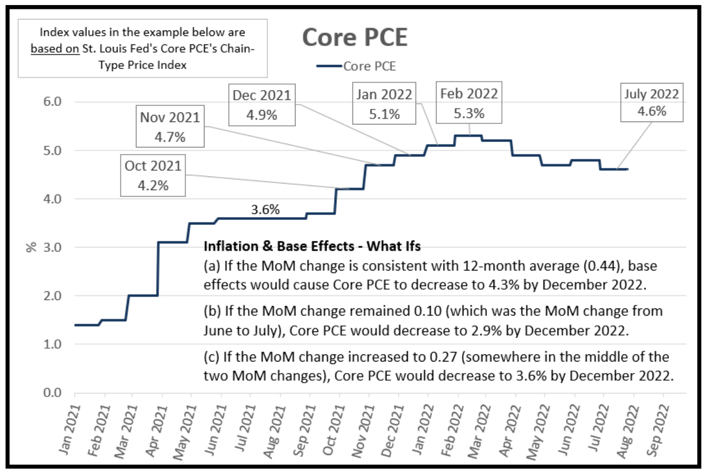
Economic Indicators:

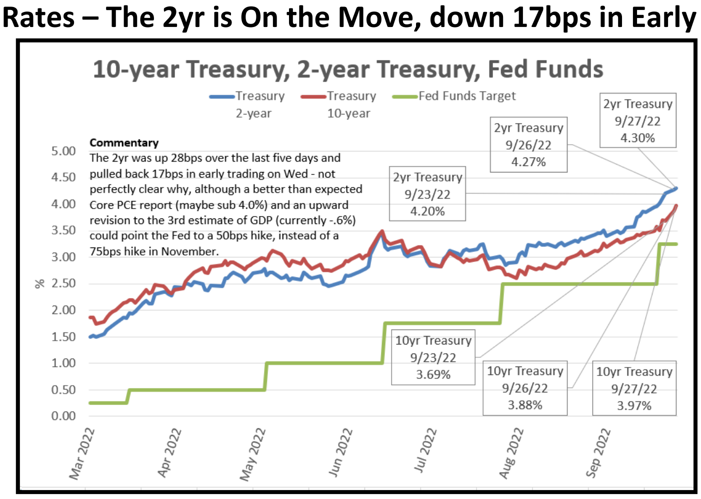
- GDP: -0.6% Q2 (2nd Est.) (Fed's Longer Run Rate 1.8%)
  - Q2 GDP (3rd Estimate) to be released tomorrow.
  - Q3 GDPNow estimate is +0.3% (posted 9/27/22).
  - Q3 GDP Adv Estimate will be released 10/27/22.
- Core PCE: 4.6% July (
  - Dallas Fed's Trimmed Mean for July: 4.40%.
    - Trims off the lower & upper data spikes.
  - St Lou Fed 5yr Breakeven Inflation Rate: 2.35%.
    - Yield on Treasury minus yield on TIPS.
  - August's Core PCE will be released Friday.
- Unemployment: 3.7% Aug (Fed's Long Run Rate: 4.0%)
  - Sept's unemployment #'s will be out 10/7/22.

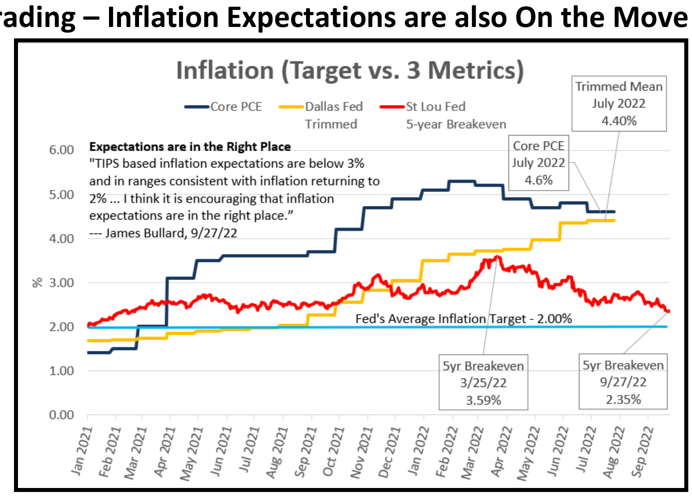


Rates --- 2-Week Trends

Key Interest Rates	9/13/22	9/14/22	9/15/22	9/16/22	9/19/22	9/20/22	9/21/22	9/22/22	9/23/22	9/26/22	9/27/22	10-Day Average	10-Day Avg vs 9/27/22	10-Day Change
Fed Funds Target Rate (FFTR)	2.50	2.50	2.50	2.50	2.50	2.50	3.25	3.25	3.25	3.25	3.25	2.88	0.38	0.75
Standing Repo Facility (SRF)	2.50	2.50	2.50	2.50	2.50	2.50	3.25	3.25	3.25	3.25	3.25	2.88	0.38	0.75
Interest on Reserve Balances (IORB)	2.40	2.40	2.40	2.40	2.40	2.40	2.40	3.15	3.15	3.15	3.15	2.70	0.45	0.75
Effective Fed Funds Rate (EFFR)	2.33	2.33	2.33	2.33	2.33	2.33	2.33	3.08	3.08	3.08	0.00	2.56	0.53	0.75
Overnight Reverse Repo Facility (ON RRP)	2.30	2.30	2.30	2.30	2.30	2.30	3.05	3.05	3.05	3.05	3.05	2.68	0.38	0.75
Fed's Balance Sheet (Total Assets in Millions)	8,822,401	8,832,759	8,832,759	8,832,759	8,832,759	8,832,759	8,816,802	8,816,802	8,816,802	8,816,802	8,816,802	8,824,564	7,762	5,599
BSBY - Overnight	2.345	2.347	2.345	2.342	2.344	2.340	2.344	2.342	2.497	3.035	3.104	2.504	0.600	0.757
BSBY - 1-month	2.673	2.719	2.770	2.856	2.893	2.918	2.983	3.025	3.053	3.086	3.108	2.941	0.167	0.389
SOFR - Overnight	2.280	2.270	2.280	2.270	2.270	2.260	2.250	2.990	2.990	2.990	0.000	2.485	0.505	0.710
SOFR - 30-Day Average	2.285	2.285	2.284	2.284	2.283	2.282	2.282	2.281	2.305	2.376	2.400	2.306	0.094	0.115
SOFR - Term Rate - 1-Month (CME Term SOFR)	2.845	2.922	3.018	3.024	3.047	3.076	3.075	3.064	3.032	3.035	3.047	3.034	0.013	0.125
US Treasury - 3-Month	3.28	3.24	3.22	3.20	3.37	3.35	3.31	3.29	3.24	3.39	3.35	3.30	0.05	0.11
US Treasury - 2-Year	3.75	3.78	3.87	3.85	3.95	3.96	4.02	4.11	4.20	4.27	4.30	4.03	0.27	0.52
US Treasury - 10-Year	3.42	3.41	3.45	3.45	3.49	3.57	3.51	3.70	3.69	3.88	3.97	3.61	0.36	0.56
US Treasury - 20-Year	3.75	3.73	3.75	3.79	3.77	3.83	3.73	3.90	3.87	4.01	4.15	3.85	0.30	0.42
3-Month / 10-year Treasury Yield Curve Spread (10yr minus 3mo Treasury) **(30yr historical avg: 1.68)**	0.14	0.17	0.23	0.25	0.12	0.22	0.20	0.41	0.45	0.49	0.62	0.32	0.30	0.45
2-Year / 10-year Treasury Yield Curve Spread (10yr minus 2yr Treasury) **(30yr historical avg: 1.14)**	(0.33)	(0.37)	(0.42)	(0.40)	(0.46)	(0.39)	(0.51)	(0.41)	(0.51)	(0.39)	(0.33)	(0.42)	0.09	0.04

Rates – The 2yr is On the Move, down 17bps in Early Trading – Inflation Expectations are also On the Move





Interesting Reads that didn't make the Report:

- KC Fed, Report: Commodity Prices Have Limited Influence on U.S. Food Inflation, 9/23/22
- Loretta Mester, Speech: Inflation, Inflation Expectations, and Monetary Policymaking Strategy, 9/26/22
- SF Fed, Report: Remote Work and Housing Demand, 9/26/22