Fed Unfiltered

WEEKLY REPORT **11/7/22**

Pete Sullivan
Rate Analyst
206-502-3811
pete.sullivan@fedunfiltered.com

Overview

FOMC – A Higher End Point & a Narrow Path to a Soft Landing

- The Fed increased Fed Funds another 75bps last week.
- In the post meeting press conference, Powell talked about a new terminal rate, "higher than previously expected" and the challenge of a soft landing as high inflation continues, "we have to have policy be more restrictive and that narrows the path to a soft landing."
  - A soft landing would be – continued growth (most analysts are expecting GDP to be 1.0% or less in 2023), higher unemployment (the natural rate is currently 4.4%) and inflation decreasing MoM for "some time".
  - The Fed's current forecast for the terminal rate or end point for this rate hike cycle is 4.6% (September's SEP).
- The Fed's blackout ended last Thursday – on Friday five Fed officials either gave a speech or were interviewed, shedding some light on the new terminal rate and what the upcoming pace of rate hikes might look like (see commentary below).

Calendar

- October's CPI report is out this week – with the supply of goods improving (supply chain issues are easing), with rate hikes softening demand (3.75% in 9-months) and with base effects (large MoM increases a year ago), October's CPI is expected to decrease – some economic analysts are forecasting CPI to be sub 3% by YE 2023 – (currently 8.2%).

November	
11/10/2022	Consumer Price Index, October 2022
11/23/2022	FOMC - Minutes of the FOMC, November 1-2, 2022
11/30/2022	Gross Domestic Product, 3rd Quarter 2022 (Second Estimate)
11/30/2022	Biege Book, October 2022
December	
12/1/2022	Personal Income and Outlays, October 2022 (aka Core PCE)
12/2/2022	Employment Situation - November 2022
12/3/2022	FOMC, Blackout Period, December 3-15
12/13/2022	Consumer Price Index, November 2022
12/14/2022	FOMC Meeting, December 13-14
12/14/2022	FOMC, Summary of Economic Projects (SEP), December 2022

Key Metrics

- Jobs – October posted job growth of 261,000, beating the median consensus (200,000) and slightly less than the 3-month average of 289,000 job growth. The unemployment rate increased to 3.7% (from 3.5%) due to a decline in the overall number of people employed (job losses without the negative job growth). Fed officials are forecasting continued increases in the unemployment rate – to 4.5% by YE 2023 (Harker, Williams) – Sept's SEP forecast is 4.4% by YE 2023.
- Up Next – Q3's 2nd estimate posts at the end of the month – no significant change from the first reading is expected.

	Current	SEP Forecast for YE22	Target or Long Run	Next Release Date
GDP	2.6	0.2	1.8	11/30/22
Core PCE	5.1	4.5	2.0	12/1/22
Unemployment Rate	3.7	3.8	4.0	12/2/22
Fed Funds (FOMC)	4.00	4.40	2.50	12/14/22

Speeches and Interviews

Evans – A Terminal Rate above 4.75% but at a Slower Pace

- "From here on out, I don't think it's front-loading anymore, I think it's looking for the right level of restrictiveness … Stepping down to a pace that's not 75, giving the Committee a little bit of runway to see more data before you get too far ahead of where you eventually want to be."
- <u>Terminal Rate</u>: "slightly higher" than 4.50% - 4.75% range.

Charles Evans, Interview: Reuters (print), 11/4/22

Barkin – Pumping the Brakes on the Way to a Higher End Point

- "You could credibly say that we have our foot on the brake … I think the implication of that is probably a slower pace of rate increases, a longer pace of rate increases and potentially a higher end point."

Tom Barkin, Interview: CNBC, 11/4/22

Kashkari – A Terminal Rate above 4.90% with Step Downs

- "I had interest rates in September peaking at around 4.9% … given what I know right now, I would expect to go higher than that. How much higher than that, I don't know."
- "Four *(75bp rate hikes)* in a row is a lot of tightening in a short period of time … At some point it will be appropriate to step down to a half point and then, at some time afterward, a quarter point"

Neel Kashkari, Interview: Associated Press (print), 11/4/22

Collins – A Higher Path if Incoming Information Supports

- "It is premature to signal how high rates should go. However, I will say that the median path in September's Summary of Economic Projections can be taken as a starting point of my current thinking, with the possibility of a higher path depending on incoming information."

Susan M. Collins, Speech/Interview: Perspectives on the Economy and Monetary Policy, 11/4/22

Reports

Jobs – The Benefits & Difficulties of the Pandemic's UI Program

- "Between March and April 2020, the U.S. economy shed 22 million jobs, a consequence of stay-at-home orders and business restrictions to slow the spread of COVID-19. In response, the U.S. embarked on an unprecedented expansion of unemployment insurance (UI) programs … for many recipients, UI payments considerably exceeded what they had earned in their previous jobs."
- "Naturally, these policy interventions have fueled a vigorous debate about the pros and cons of more generous UI benefits and, in particular, the extent to which they have contributed to labor supply shortages, thereby slowing down the recovery."
- <u>Conclusion</u>: "Pandemic UI supplements affected the labor market in two ways: (1) On one hand, they made it difficult for stores — especially low-paying stores — to find workers; (2) On the other hand, they supported local demand by raising the disposable income of the unemployed."

Richmond Fed, Report: How Did Pandemic UI Benefits Affect Employment Recovery in Local Industry Markets? 11/4/22

Trends

Rates were up last week – mainly due to the Fed's expected and then actual rate hike on Wednesday – Friday's unemployment report was likely the cause of the slight pull back on Friday – the reality of rate hikes likely sinking in – including the potential for job losses, a higher unemployment rate and the possibility of a recession – the most reliable indicator of an upcoming recession (3m/10yr spread) continues to be inverted, although if the 3-month treasury remains flat and the 10-year continues its slow upward trend, the inversion could correct itself – the question then becomes, is a recession still less than 12-months away if the 3m/10yr inverts only briefly (currently a 9-day inversion)?

Key Interest Rates	10/31/22	11/1/22	11/2/22	11/3/22	11/4/22	5-Day Change
Fed Funds Target Rate (FFTR)	3.25	3.25	4.00	4.00	4.00	0.75
BSBY - Overnight	3.099	3.109	3.111	3.117	3.228	0.129
BSBY - 1-month	3.634	3.657	3.732	3.803	3.840	0.206
SOFR - Overnight	3.050	3.050	3.050	3.800	0.000	0.750
SOFR - 30-Day Average	3.037	3.040	3.042	3.044	3.069	0.032
SOFR - Term Rate - 1-Month	3.761	3.786	3.782	3.794	3.807	0.046
US Treasury - 3-Month	4.22	4.23	4.22	4.25	4.21	(0.01)
US Treasury - 2-Year	4.51	4.54	4.61	4.71	4.66	0.15
US Treasury - 10-Year	4.10	4.07	4.10	4.14	4.17	0.07
US Treasury - 20-Year	4.44	4.37	4.41	4.42	4.49	0.05
YC Spread - 3-Month / 10-year Treasury	(0.12)	(0.16)	(0.12)	(0.11)	(0.04)	0.08
YC Spread - 2-Year / 10-year Treasury	(0.41)	(0.47)	(0.51)	(0.57)	(0.49)	(0.08)

Quote of the Week

"In the middle of every difficulty, lies opportunity."
--- Albert Einstein