First Trust
Monday Morning OUTLOOK

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50 or More?

All eyes will be on the results of the Federal Reserve meeting on Wednesday when it announces how much it's going to raise short-term rates, its new projections for the economy and short-term rates for the next few years, as well as Chairman Powell's press conference.

After the last meeting in May, Powell made it very clear the Fed anticipated raising rates by half a percentage point (50 basis points, or bps) at each of the next two meetings: this week's event and in July. When asked about a larger rate hike, Powell was dismissive.

But after Friday's news that consumer prices rose 1.0% in May and are up 8.6% versus a year ago – the most in more than forty years – the futures market in federal funds is pricing in moves of *at least* 50 bps this week and in July.

A widely known investment TV celebrity says the Fed should go 100 bps all at once on Wednesday. We would fully support a 100 bps rate hike this week, or even more. In fact, we were calling for an even sharper rate hike and a faster pace of Quantitative Tightening back in March, before it was cool to act tough.

We would not be shocked if the Fed raised rates by more than 50 bps on Wednesday but think it will more likely stick with 50 bps only. Why? Remember that Powell was emphatic back in May that the Fed did not need to go 75 bps at the next meeting. Moreover, Powell puts a great deal of weight – way too much, in our view – on gradualism and signaling rather than just focusing on getting monetary policy to where it needs to be to achieve the goal of getting inflation under control.

To Powell, if the Fed ends up raising rates by 75 bps or more this week, it'd mean he wouldn't be able to accurately signal the pace of future rate hikes the way he wants. Again, we don't think that should matter nearly as much as getting monetary policy right, but we think signaling ability is important to him.

Instead of getting 75 bps or more on Wednesday, pay close attention to what Powell says about the size of the likely rate hike in July and the months beyond. We anticipate that he will show more openness to larger rate hikes this week than he did back in May. Given the stubbornly high path of inflation, he probably regrets being so dismissive about a rate hike of 75 bps or more back in May.

Either way, we think the market needs to focus on not only what happens on Wednesday but what happens on June 28. That's the day, at Noon Central Time, the Fed releases its monthly figures on measures of the money supply. In the current economic environment, that news should be at least as important as what the Fed does with interest rates.

The Fed used to implement monetary policy by using open market operations to add or drain reserves from the banking system, thereby controlling interest rates. That all ended around the time of the Financial Crisis in 2008. Now the Fed adjusts short-term rates directly.

But we believe it's the growth of the M2 measure of the money supply that determines the pace of inflation. And no one knows how effective, under the new post-2008 regime, raising rates will be to keep M2 growth in check enough to bring down inflation. Only time will tell. Either way, we anticipate lots more rate hikes and Quantitative Tightening before the Fed wrestles inflation back down to its 2.0% goal.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
6-14 / 7:30 am	PPI – May	+0.8%	**+0.9%**		+0.5%
7:30 am	"Core" PPI – May	+0.6%	**+0.6%**		+0.4%
6-15 / 7:30 am	Retail Sales – May	+0.1%	**+0.3%**		+0.9%
7:30 am	Retail Sales Ex-Auto – May	+0.7%	**+1.1%**		+0.6%
7:30 am	Import Prices – May	+1.1%	**+0.4%**		0.0%
7:30 am	Export Prices – May	+1.3%	**+0.6%**		+0.6%
7:30 am	Empire State Mfg Survey – Jun	3.0	**5.9**		-11.6
9:00 am	Business Inventories – Apr	+1.2%	**+1.2%**		+2.0%
6-16 / 7:30 am	Initial Claims – Jun 12	215K	**222K**		229K
7:30 am	Housing Starts – May	1.700 Mil	**1.710 Mil**		1.724 Mil
7:30 am	Philly Fed Survey – Jun	5.0	**17.0**		2.6
6-17 / 8:15 am	Industrial Production – May	+0.4%	**+0.4%**		+1.1%
8:15 am	Capacity Utilization – May	79.2%	**79.3%**		79.0%