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MACRO MORNING BRIEFING

June 12, 2024

Sussing Out The Fed's New SEP

Fewer cuts, higher inflation, and a small contradiction

- The FOMC now sees only one rate cut in 2024
- Its projection for the terminal rate moved higher
- A seeming contradiction in the dots: higher inflation this year *and* rate cuts
- We remain firm in our call for a rate cut in September

Mildly Hawkish Dot Plot

Wednesday's FOMC announcement and press conference focused mainly on changes in some of the key elements of the June Summary of Economic Projections (SEP, "the dots"). We expected some of the nearly four rate cuts indicated in the March (and December) SEP to be eliminated, and for the new projection for the end-2024 funds rate to move higher. Check and check. Some noteworthy items in the June SEP summarized:

- 2024 federal funds rate: The dot for this item was raised a bit more than we expected. In our FOMC preview we expected to see a total of 1.5 to 2 rate cuts, but the SEP reported just one cut (of 25bp) expected.
- However, among the 19 submissions for the 2024 dot, 8 members projected two cuts, 7 members projected one cut, and 4 projected zero cuts. The plurality of the dots was therefore in favor of reducing the policy rate by 50bp this year, and a healthy majority saw at least one cut.
- The projection for the "longer term" federal funds rate, a proxy for the neutral rate of interest, or r*, moved higher, from 2.6% to 2.8%. This is still lower than our own view of the equilibrium policy rate (see here) but indicates there is some movement amongst

the FOMC on this topic. In his press conference, Chair Powell dismissed r* as a "concept", not a number that lends itself to be precisely estimated a priori.

Although the rate-cut view was more hawkish than in the March SEP, we think the details moderate that hawkishness. Chair Powell offered little new in his press conference.

In our FOMC preview we also indicated interest in the growth and unemployment rate projections, which we thought might offer insight into how the Fed views the current state and expected evolution of the economy this year. Other than moving PCE forecasts higher, core to 2.8% by year-end, growth and unemployment projections were unchanged.

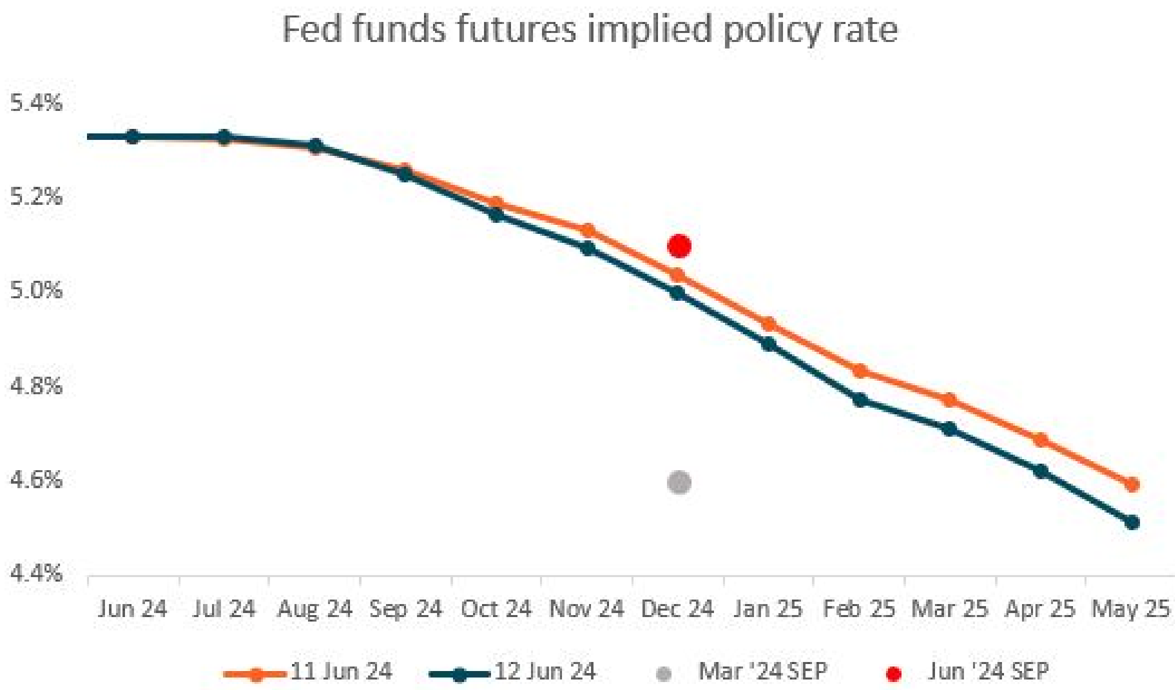
Speaking of the higher PCE projection, we – and others – noted a seeming inconsistency in the 2024 dot plot as a collection. Rate cuts are still expected, even if just one, yet inflation is seen rising slightly by year-end, with growth and unemployment unchanged. In other words, the median Committee member sees lower rates, yet higher inflation and no slowing in the economy. One wonders how that holds together. Powell didn't really have a good answer to that question. We don't, either.

We still see a rate cut in September, although recognize the oft-stated need for greater confidence. This means inflation data – CPI, PCE, wages, and other price measures) – continue to be the most important information for gauging the future course of rates.

On that note, today's CPI report was worth celebrating for the moment, although, as stated above – and also by Powell – greater confidence is indeed needed. We think that confidence will come over the next few months. It seems the dovish message from the CPI print was more powerful than the slightly hawkish one from the Fed, with the morning's market reaction to the inflation report not being close to undone after the FOMC.

The market is now — as it was when rates were rising — more dovish than the Fed, as the chart below shows. Unlike on the way up, we tend to agree with Tuesday's end-of-day federal funds futures curve, which sees about two full 25bp cuts by the end of the year. We also think the data will soon the provide greater confidence the Fed needs.

Market Versus Fed



Source: BNY Markets, Bloomberg, Federal Reserve Board of Governors

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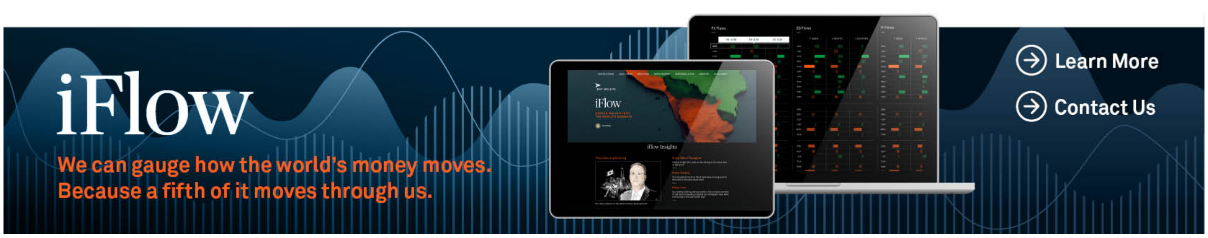

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