Rodney's Take
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What if They're Wrong?

The unemployment rate remains low, there are more than two job openings for every unemployed person, and inflation remains above 8%. The Federal Reserve just raised rates by another 0.75%, and Chair Powell told reporters that the speed at which the central bank raises rates isn't as informative as the overnight rate they eventually will reach. Powell reiterated several times that they will raise rates to whatever level is needed to bring inflation to its 2% target and that he expects the process to be painful. Investors took his comments to heart and sold off the markets, but I'm not so sure. What if the central bankers are wrong again?

The Fed releases an economic forecast every three months. In March 2021, the bankers expected the overnight rate to be 0.1% through 2023. Just 90 days later, they bumped their forecast a bit, leaving the forecast for the overnight rate at 0.1% in 2022 but pushing the rate to 0.6% in 2023. By December of last year, with the Personal Consumption Expenditures Price Index (the Fed's preferred inflationary index) at a 40-year high of 5.7% in November, the bankers raised their 2022 overnight rate forecast to a whopping 0.9% and their 2023 forecast to 1.6%.

In their quest to slay inflation, it's likely that the Fed will have raised the overnight rate to at least 4.25% by the time we close out this year. My, how times (and the views of the Fed) change.

I don't bring this up to flog the central bankers. I'm just pointing out that they can be wrong and can adjust their actions to fit the data. I've said many times that much of what the Fed is fighting is supply inflation that it didn't create, not demand inflation dependent on borrowed money. The central bank didn't snarl the global supply chain, it didn't send trillions of dollars to consumers and hundreds of billions of dollars to cities and states, it didn't discourage domestic energy production, and it didn't encourage Russia to invade Ukraine. The Fed did give newly remote employees the ability to secure mortgages with rock-bottom rates, which they used to push prices on our limited housing stock to the moon, but that's just one facet of the economy.

I don't see inflation turning into deflation in the next six months, but with most prices only modestly higher in recent months and rents turning lower, inflation could be cut in half and then some. If that comes to pass, then central bankers will be holding overnight rates higher than the inflation rate, the yield curve will invert, and investors will be scrambling to position themselves for the Fed pivot or at least the Fed plateau. The central bankers likely won't lower rates quickly so that they can make sure the inflation monster is dead, but that won't matter to equity buyers, who won't want to miss the big run.

Remember the advice of hockey great Wayne Gretzky. Don't skate to where the puck *is*, skate to where it's *going to be*.

Rodney

Got a question or comment? You can contact us at info@hsdent.com.