Rodney's Take

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Calling BS on our Profession

My job is to give you a reasonable forecast of where parts of the economy are headed. From interest rates to GDP growth and from demographics to jobs, I stay informed on a lot of stuff. My particular passion is sifting through the "what ifs," the long-tail possibilities that aren't mainstream but have enough merit to be worth considerable thought. I know that's nerdy, but we all need a reason to get up in the morning, which brings me to the huge topic for today, interest rates. They are very important, and yet we don't know where they are going. We don't have a clue.

The Fed took interest market pricing away from investors. People who say otherwise are kidding themselves, at best.

In 2008, the Fed started printing money to buy down long rates. It worked, but by late 2014 it left the central bank with $4.5 trillion on its books. The Fed rolled off just $750 billion between December 2017 and September 2019 when the economy wobbled. That showed us that the central bankers are weak hands, ready to rescue GDP at a moment's notice. Then came the pandemic and another $5 trillion. Jay Powell and his merry band pledged to wind down the program, and they at least started to do so. They let their bag of stash dwindle from $8.9 trillion to $8.4 trillion after a few banks blew up in March. The Fed immediately bought $400 billion back.

Since then, the central bankers have allowed $600 billion to mature off of the Fed books while lecturing us about throttling inflation. Hmm. I'm not so sure.

The Fed runs a reverse repurchase agreement program (RRP) that allows people who want to own Treasury bonds of any maturity to do so on the same terms as overnight federal funds. While the Fed is beating its chest about slaying the inflation dragon, we've also seen $600 billion bleed out of the RRP, with a lot of it ending up in regular short-term bonds. The key term here is "short term." While bankers have made noises about holding rates higher for longer, and I subscribe to that view, I think they will fold like a cheap suit if things get tough and inflation remains high.

If short-term bond rates fit your investment goals, then great. I think you'll be content for six to nine months. But make a plan for what you want to do when the Fed changes its mind, lowers short-term rates dramatically, and crams down long rates by bloating its balance sheet. I am certain they will; I just don't know when.

Rodney Johnson

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