



# Higher for Longer The Long Wait for the First Cut

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# Growth is Accelerating

- Consumption is strong
- 2022's weak sectors recovering
- Lower inflation boosts real income
- Fiscal policy highly stimulative





# Economy continues to run hot

Recession fears were overblown, economy beating forecasts

### Bloomberg Economic Surprise index

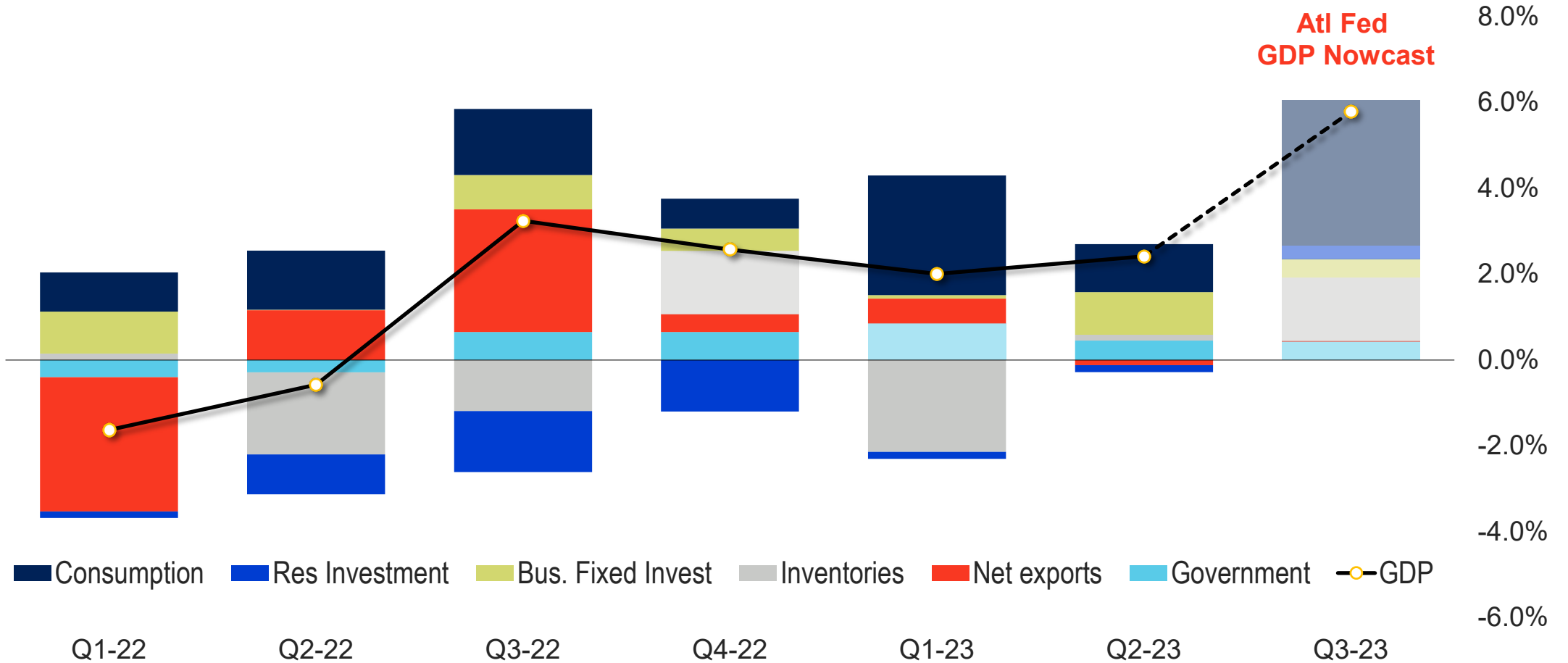


# GDP accelerated in Q2; off to strong start in Q3

Business investment and consumption benefit from federal stimulus

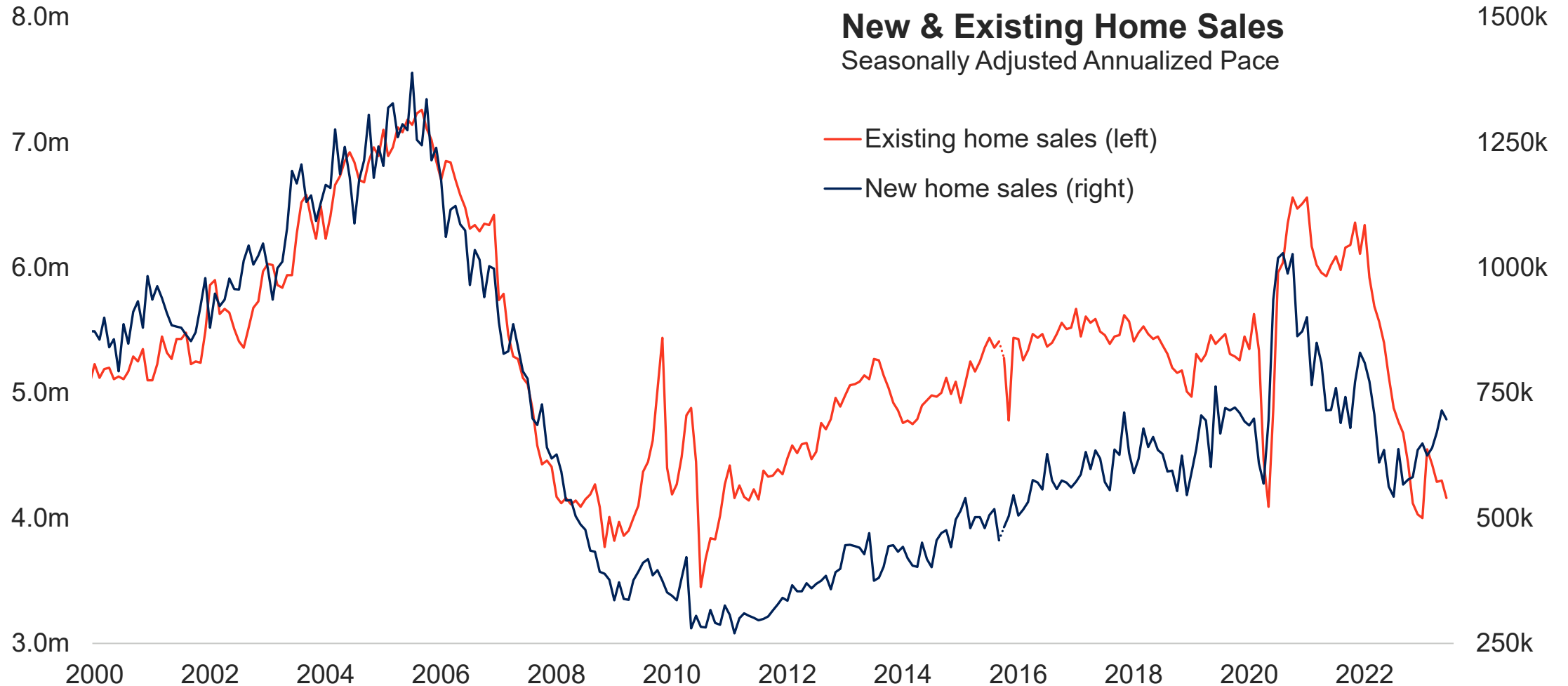
## Real GDP Growth

Qtr/Qtr% Annualized with Sector Contributions



# Home sales stabilizing despite high rates

Mortgage rates near 7% don't deter buyers. How about 7.5? 8%?



# Inflation Is Falling

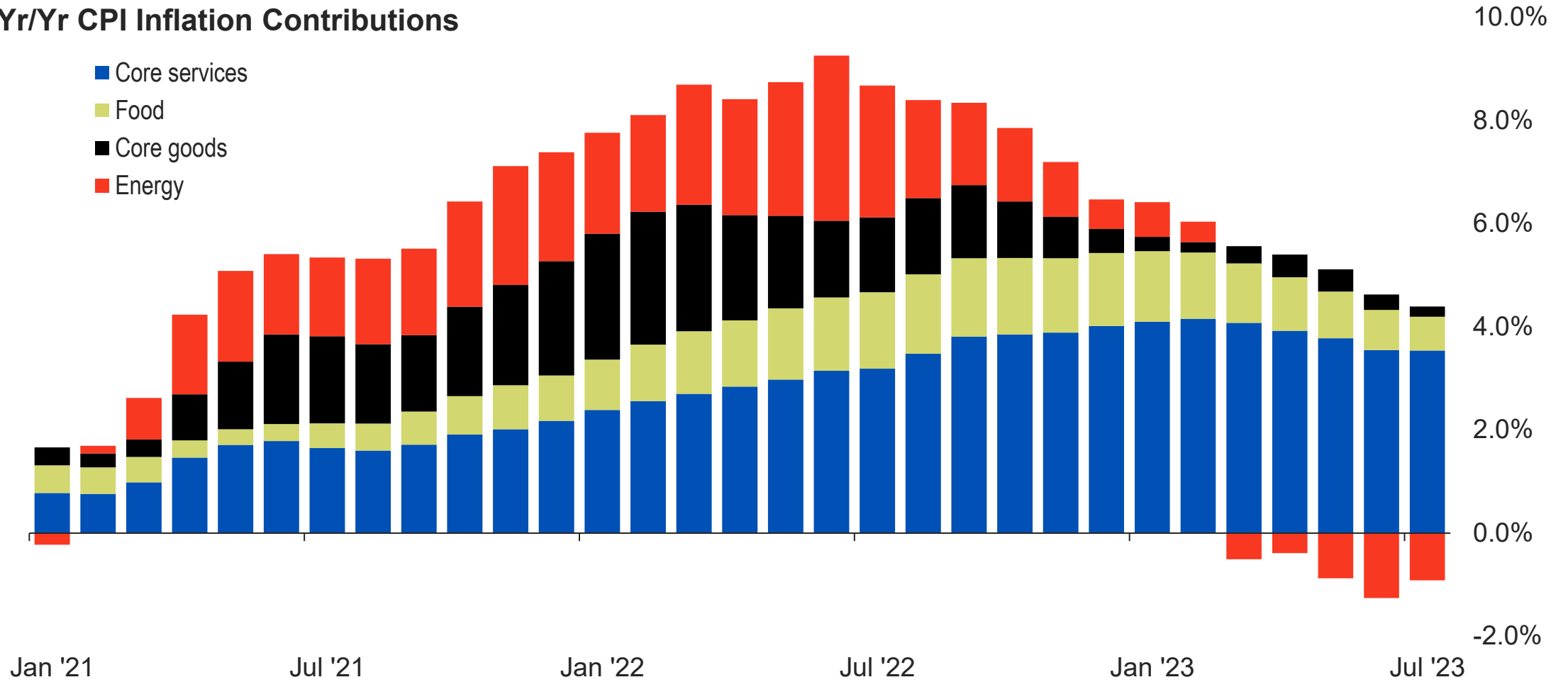
- Inflation moderating. But:
  - Supply-chain healing ending
  - Cyclical inflation resurgent
- Core inflation falling very slowly
- Energy inflation is back
- Fed watching speed and magnitude of inflation drop



# CPI inflation fell through first half

Energy and core service pressures starting to build again

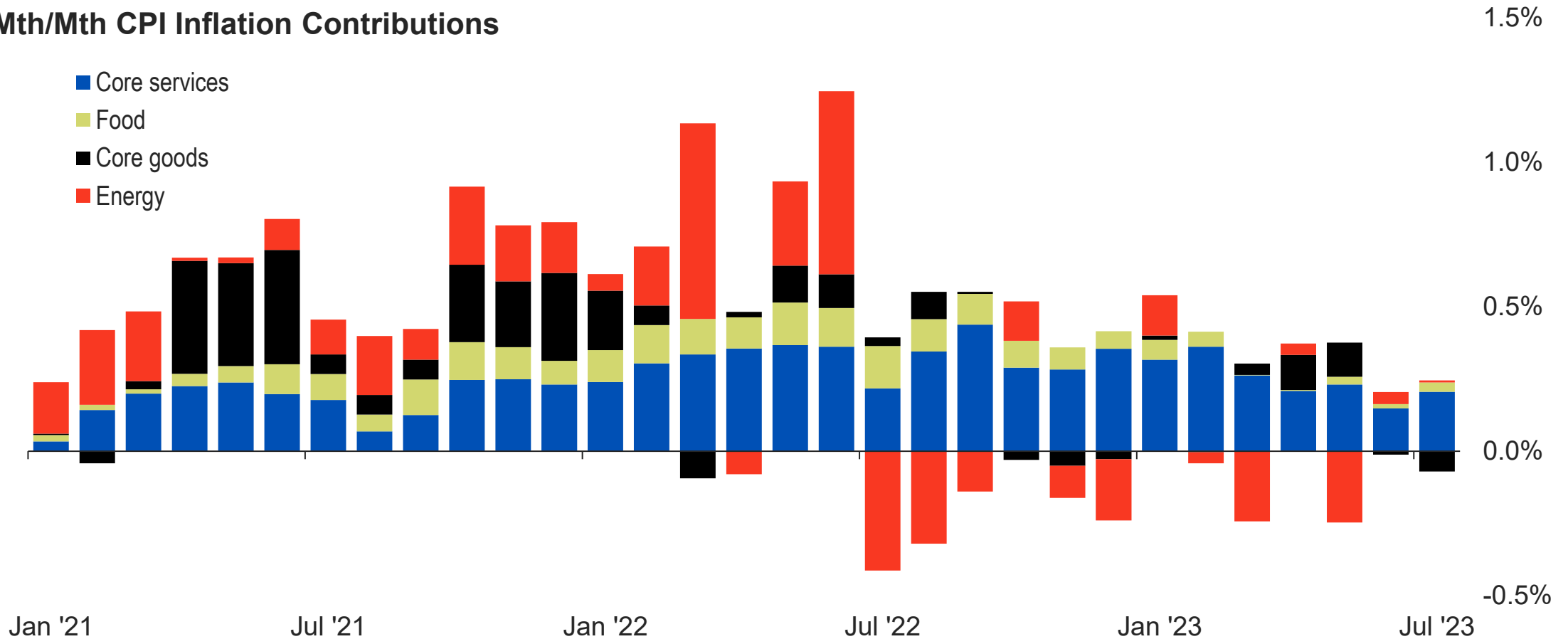
## Yr/Yr CPI Inflation Contributions



# CPI inflation fell through first half

Monthly inflation numbers less directional recently, suggesting conflicting undercurrents

### Mth/Mth CPI Inflation Contributions

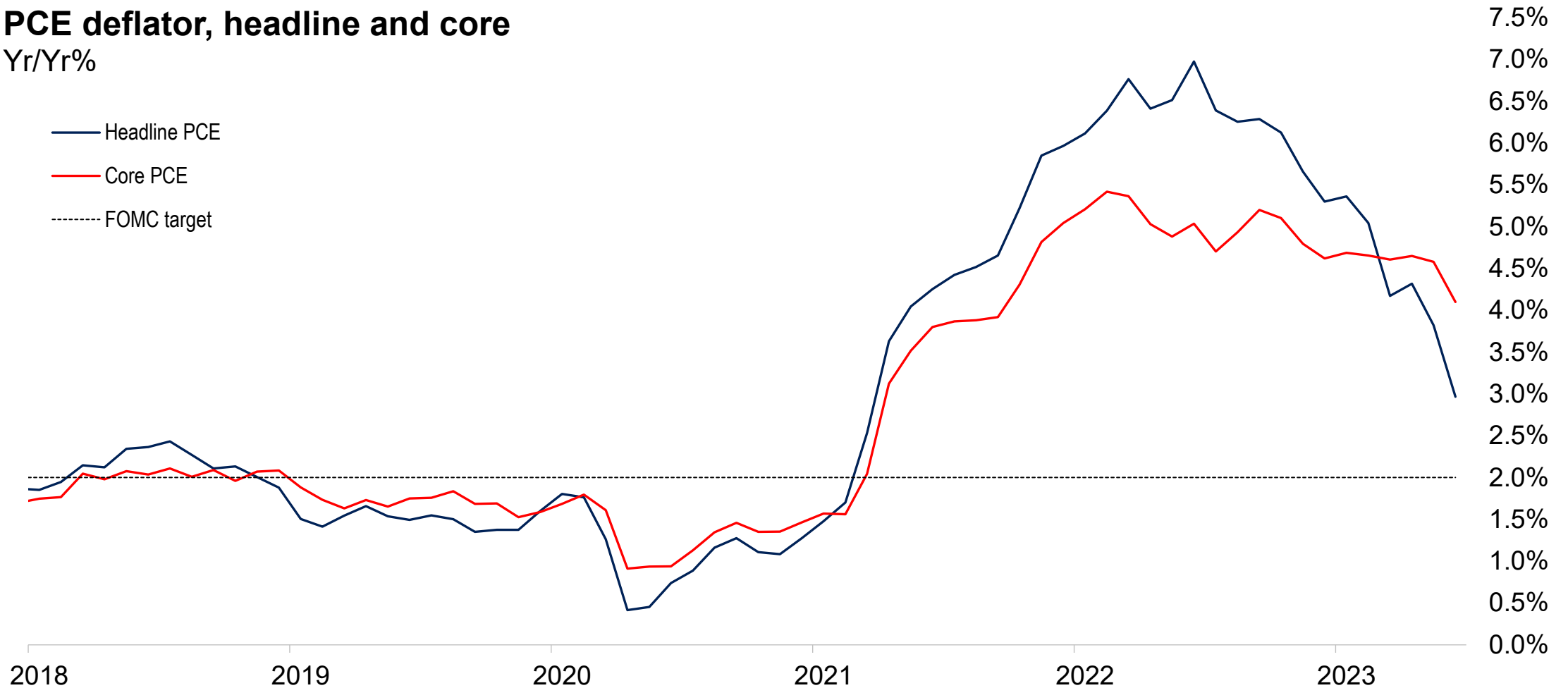




# Inflation tumbled in June

Most significant monthly improvement yet

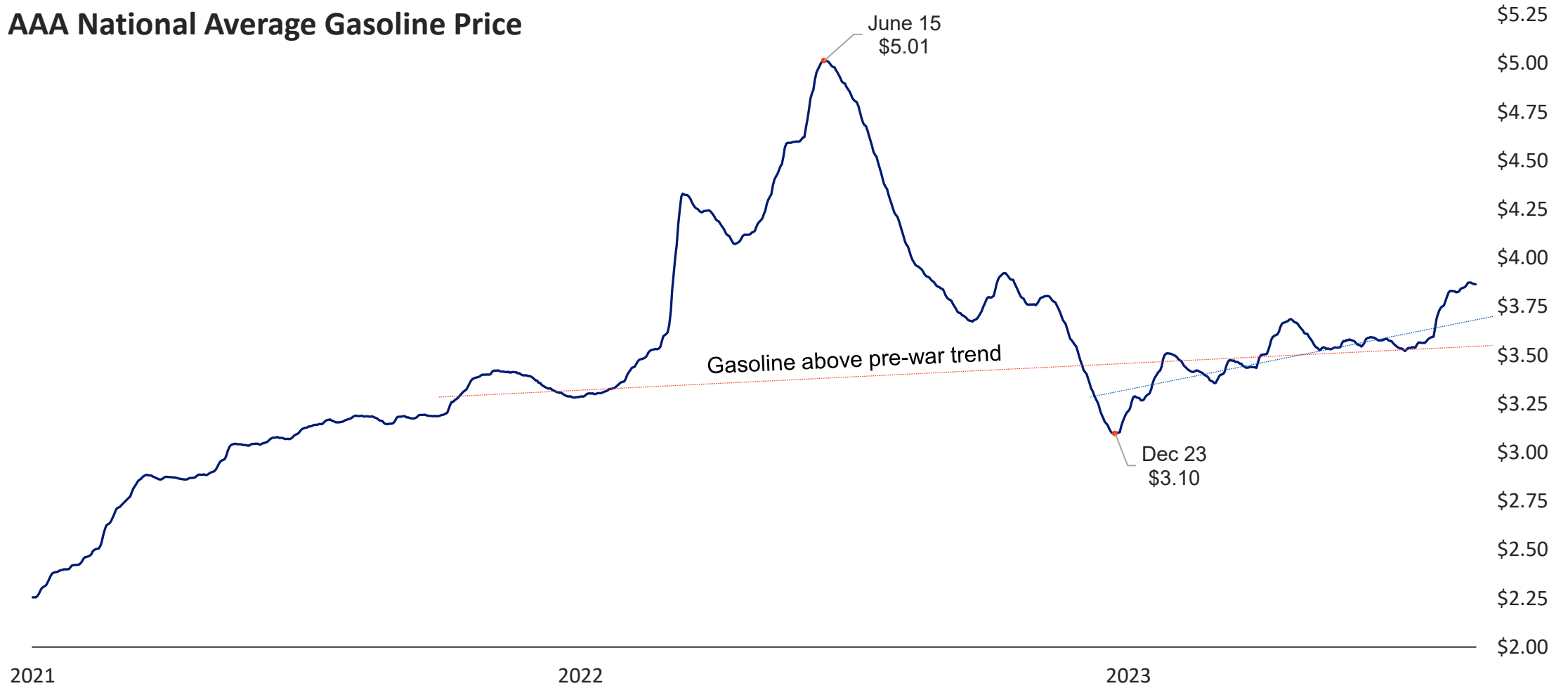
## PCE deflator, headline and core Yr/Yr%



# Easy energy disinflation is over

Russian invasion's influence ended last December

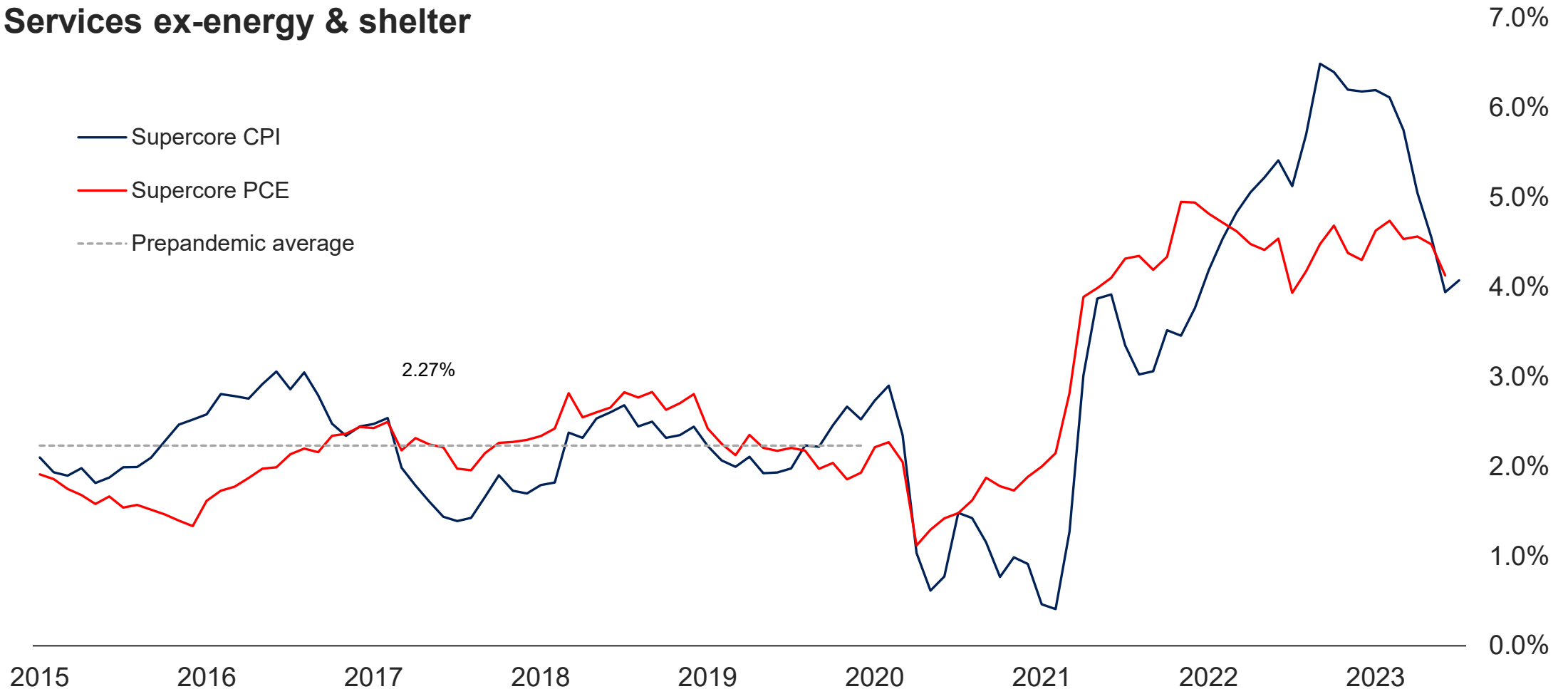
## AAA National Average Gasoline Price



# Supercore is where PCE and CPI diverge most

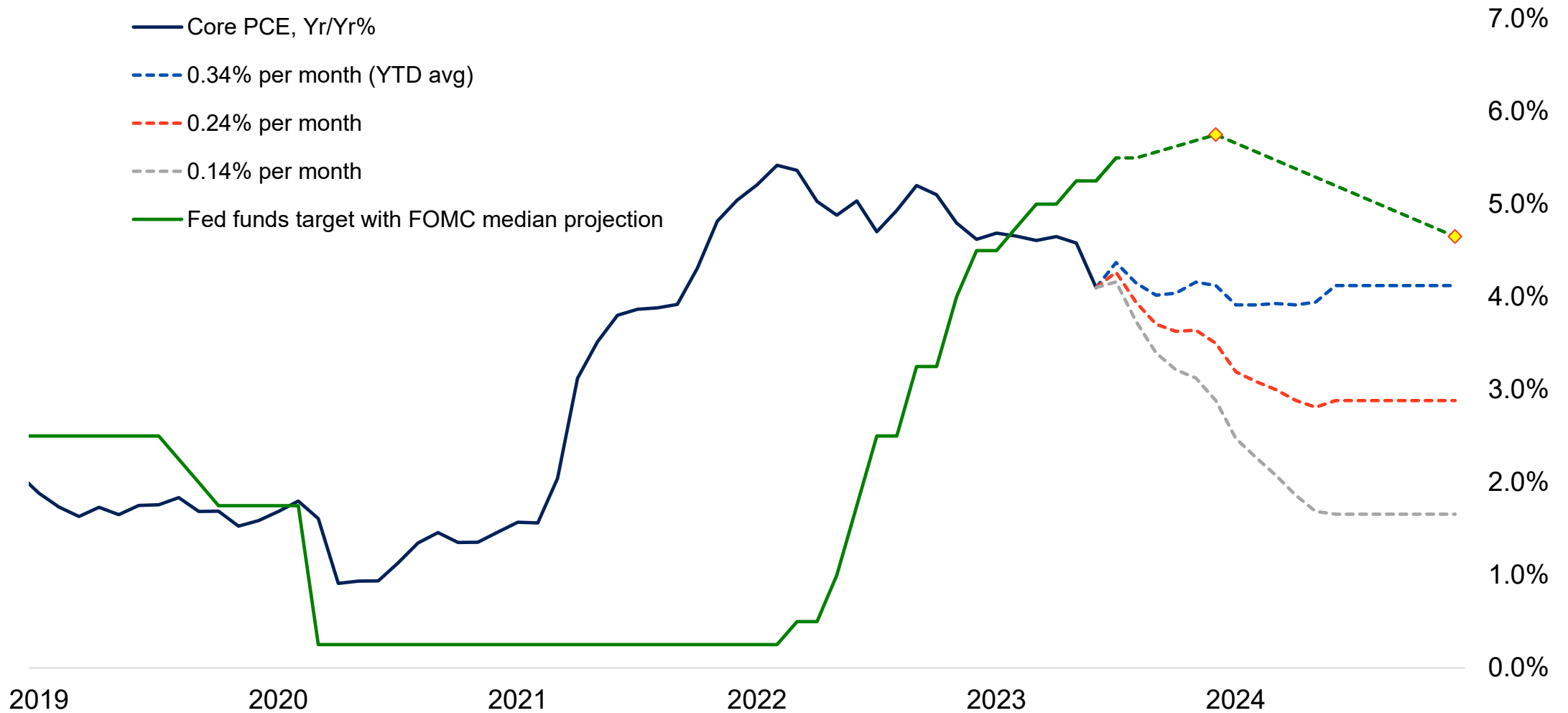
More rapid CPI improvement comes from measurement differences

## Services ex-energy & shelter



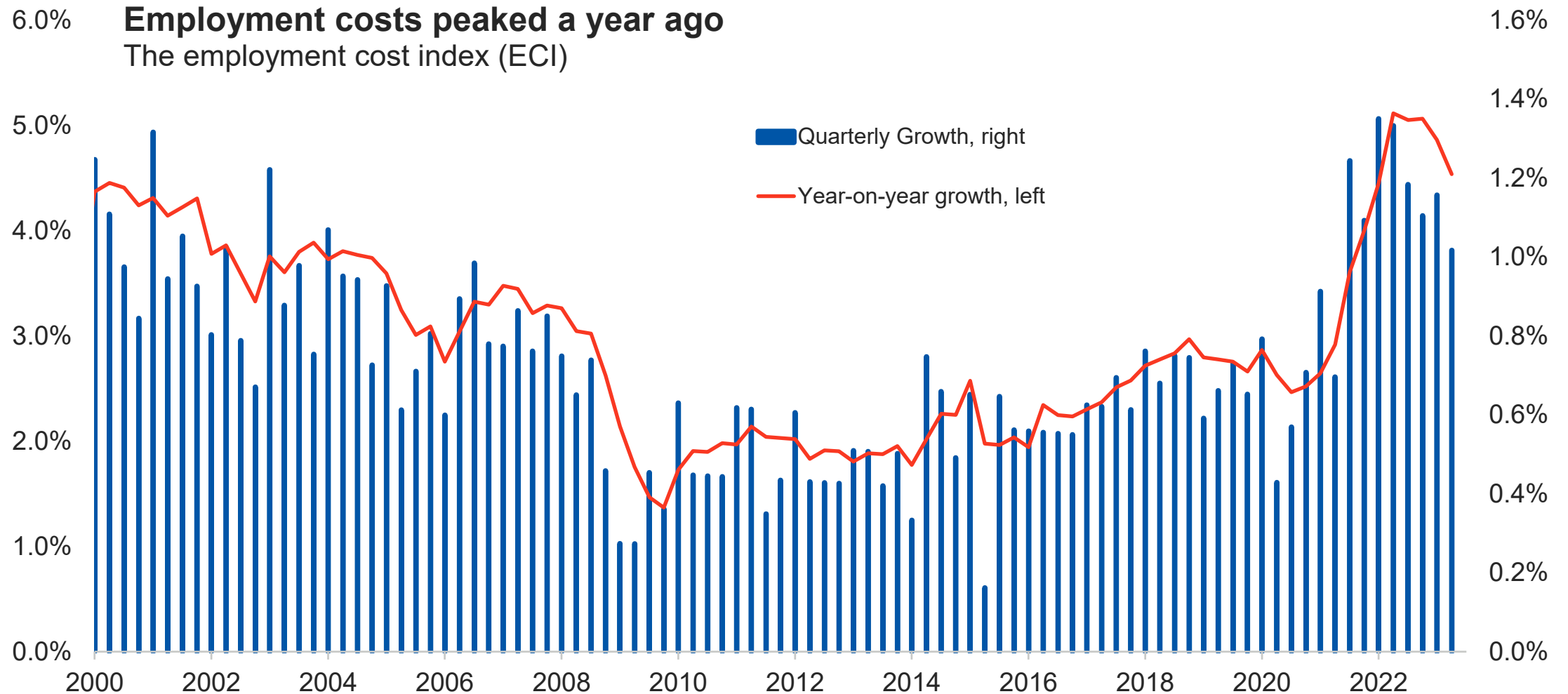
# Inflation "What if?"

Easy improvements are behind us



# Employment costs are moderating, too

ECI was icing on inflation cake in June





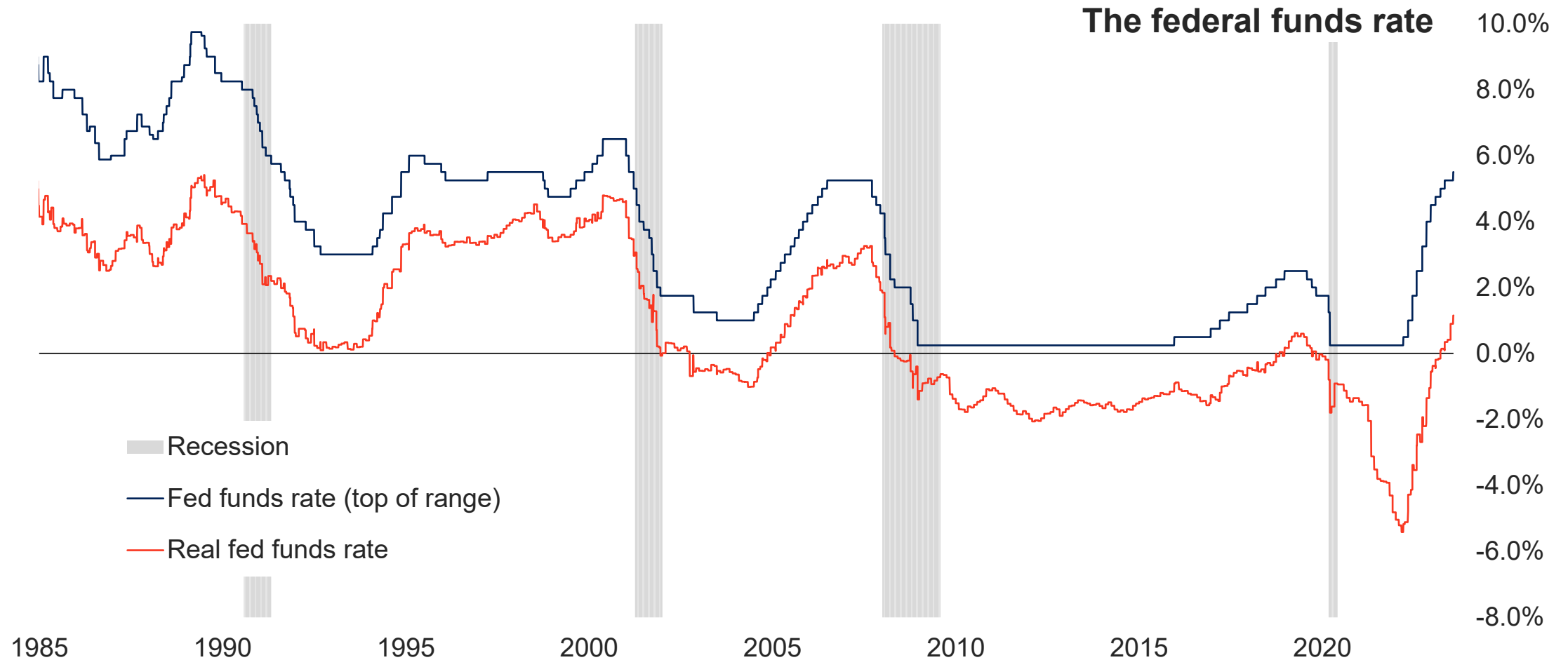
# Monetary Policy and Interest Rates

- Fed determined to keep inflation falling
- Policy already restrictive
- Market (sort of) betting against more hikes
- September live; brings new dot plot



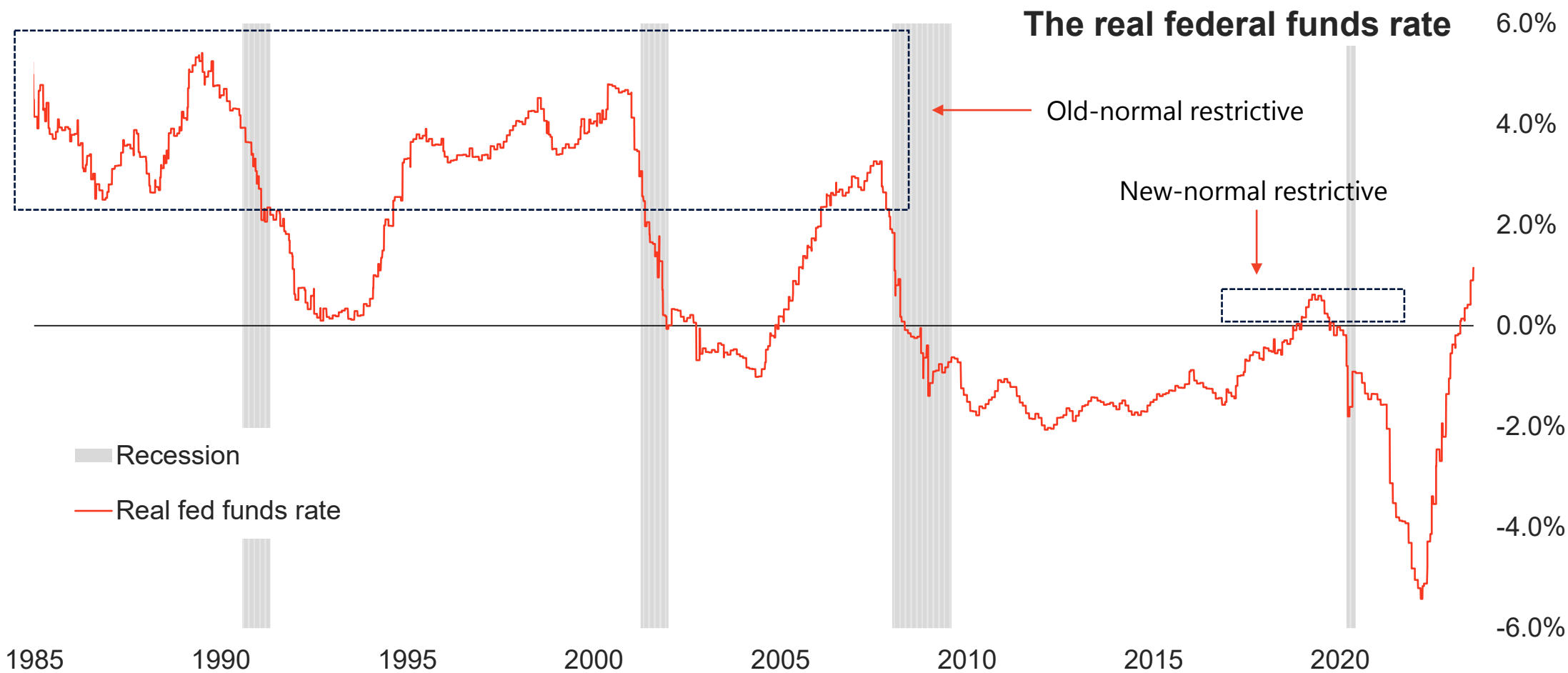
# Highest fed funds rate in 22 years. Or, is it 14?

Powell stressed importance of the real rate; but where is the new, new normal?



# Return of the Old Normal?

2010-2019 was the post-GFC outlier of past 50 years



# I The path to easing

Jay Powell explains what the Fed needs to see to cut rates

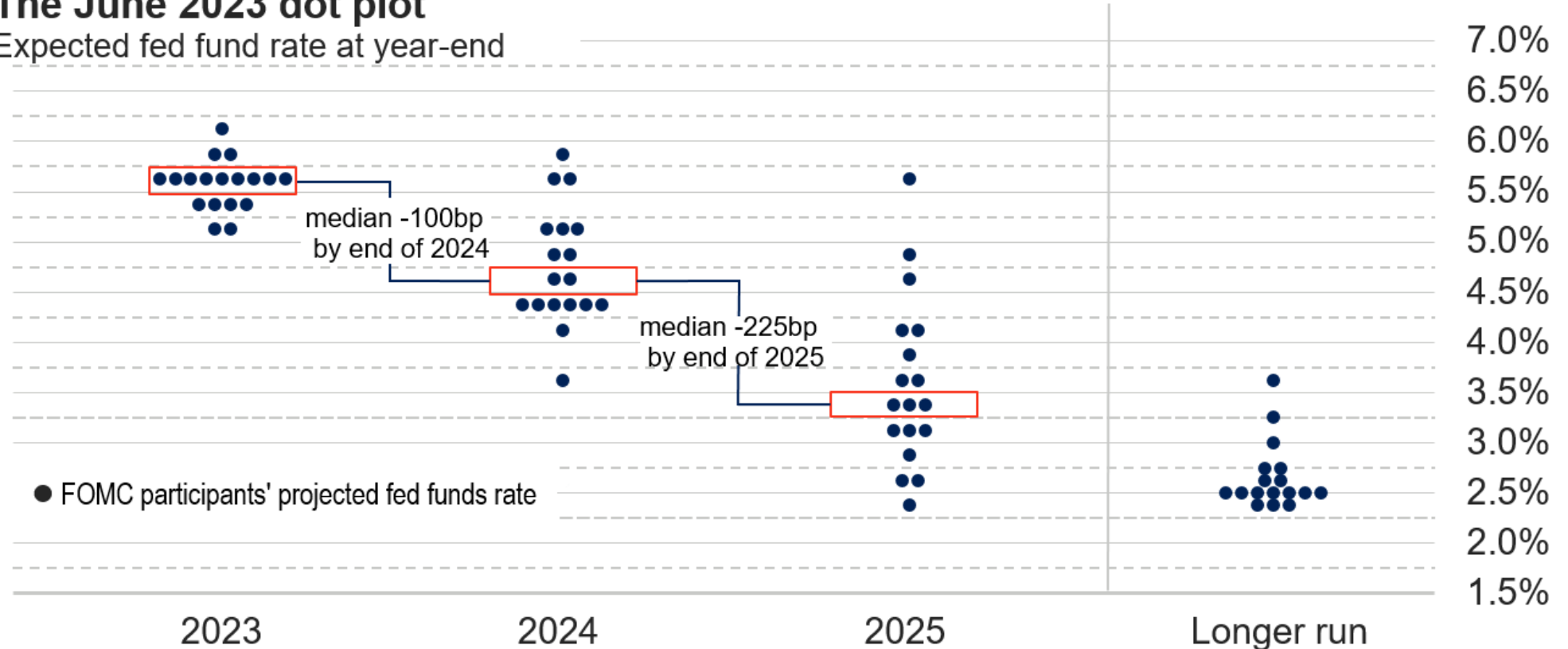
- Policy is restrictive
- Higher rates would make it more restrictive; so would lower inflation
- FOMC will pause “long before inflation returns to 2%”
- Extended pause? Yes, if recession is avoided
- FOMC will cut rates before inflation reaches 2%; “couple of years out”
- Rate cuts could happen even if Fed is still engaged in QT

# June dots suggest one more hike, cuts next year

Median drops considerably in 2024 and '25, but uncertainty rises, too

## The June 2023 dot plot

Expected fed fund rate at year-end

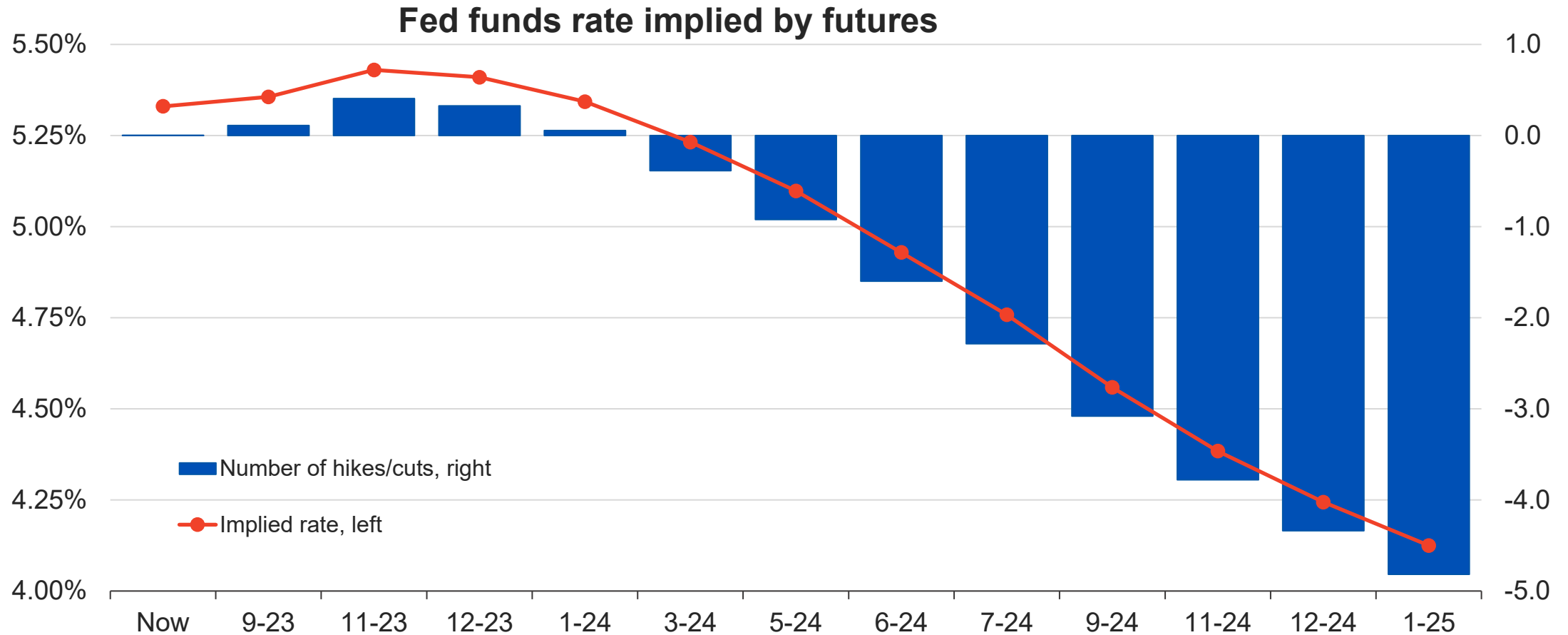


Note: Each dot represents the expectations of one FOMC member. Median projection is 5.6% for 2023, 4.6% for 2024 and 3.4% in 2025. The longer run median is 2.5%. One member did not submit projections for the longer run.



# Bloomberg interest rate probabilities

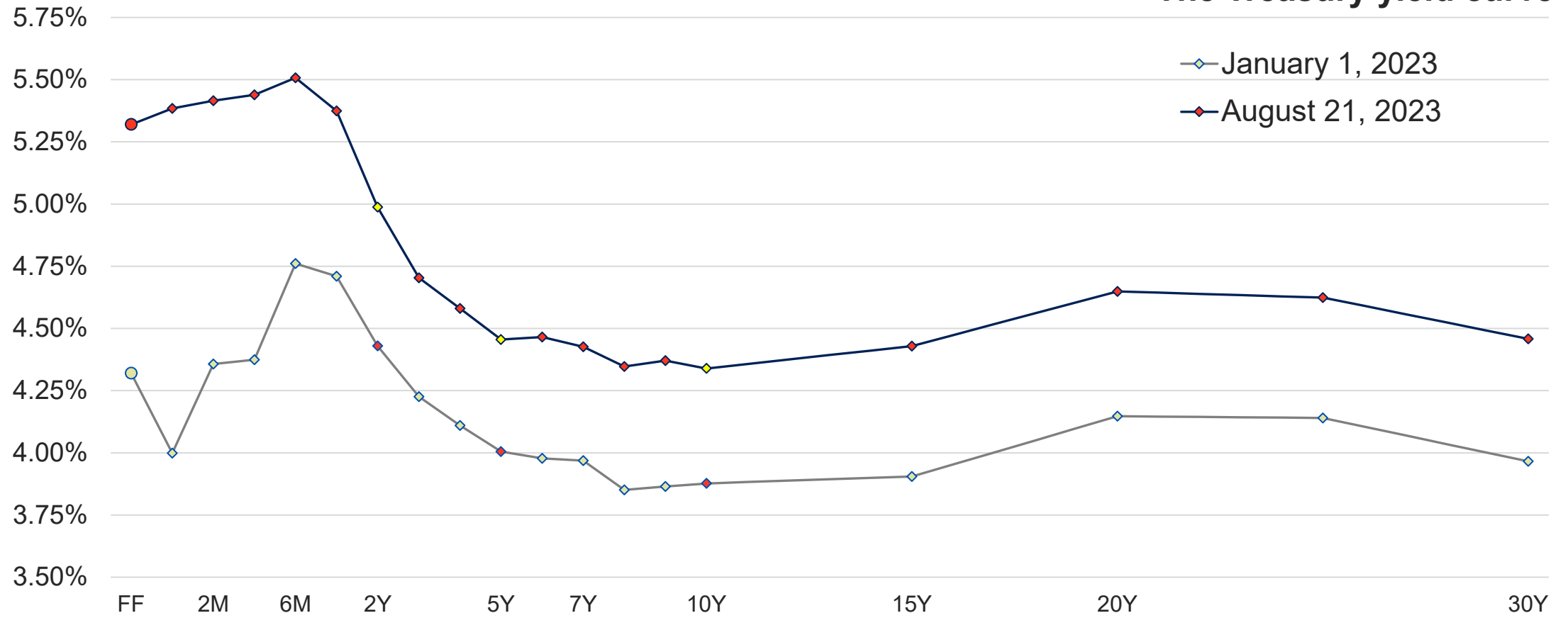
Fed funds futures market sees little chance of further hikes



# Cash Treasuries braced for another hike

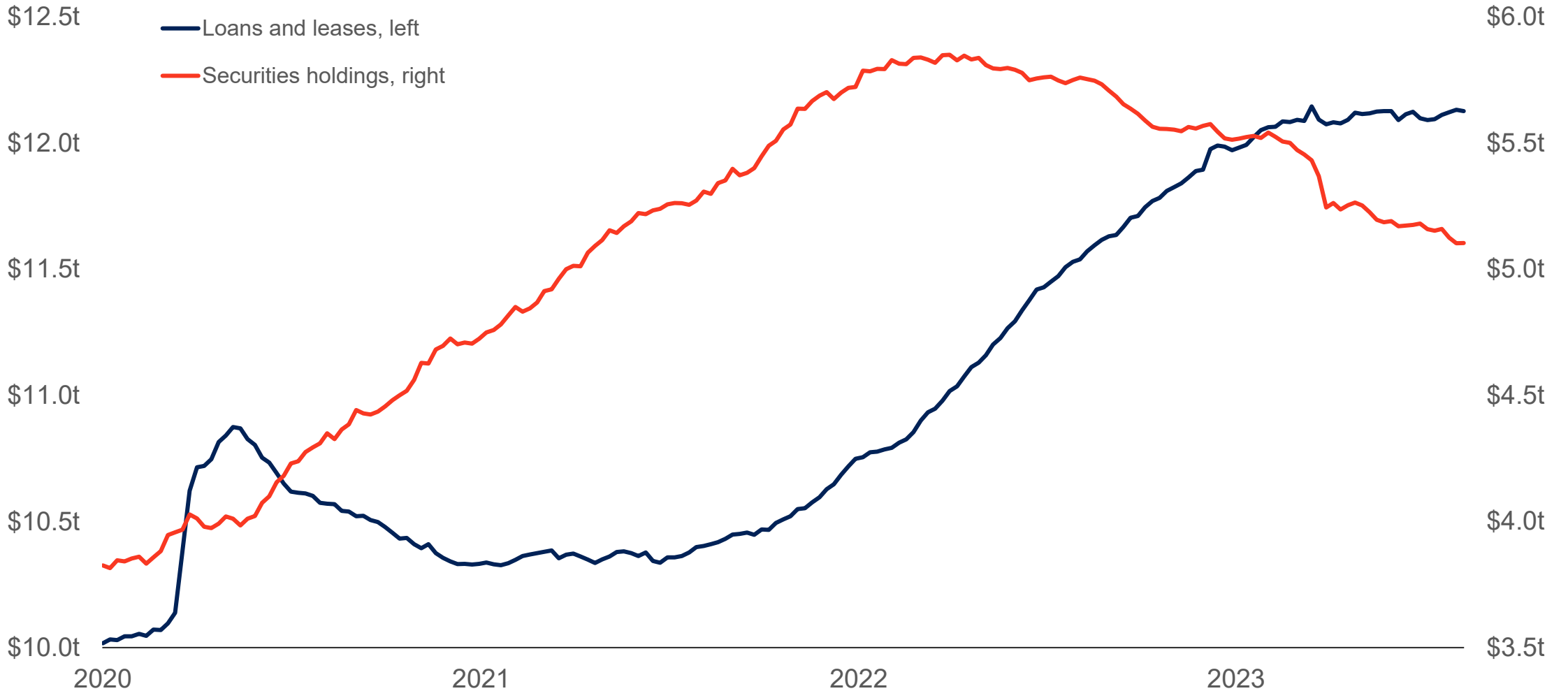
Yield curve is priced to Fed dot plot

### The Treasury yield curve



# Banks starting to restrict lending

Banks are cutting assets, though mostly by running off securities



# I Cyclical now drive inflation

Pandemic and war effects are finally giving way to more traditional inflationary behavior

- GDP faltered last year, but is re-accelerating now
- Atlanta Fed initial Q3 Nowcast 3.5%. Now 5.8%!
- Inflation drop to 3% benefitted from falling energy prices
- Core dropping VERY slowly
- Powell is right. Soft landing is possible, not most likely
- Next few months are critical



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