

# MARKET COMMENTARY

Fed: Powell reminds that further hikes are possible

**Paolo Zanghieri**

**August 25, 2023**

- **Today' Jackson Hole speech allowed chair Powell to cautiously add a slightly hawkish touch to main messages conveyed since July. Inflation is receding but still too high and may require further rate hikes and/or a longer period of tight policy.**
- **He pointed to upside risks to inflation stemming from still above trend growth and a still tight labour market. However, he also acknowledged the high uncertainty on the actual stance of monetary policy and the size of the policy lags. Therefore, the FOMC keeps refraining on any commitments.**
- **We think the hawkish tilt was mainly meant to dash residual hopes of swift rate cuts. We stick to our view of no more rate hikes, but we move to Q2 the date of the first cut. Only surprisingly strong readings in the next employment and CPI reports would warrant a rate hike in September.**

Chair Powell's speech at the Jackson Hole did not provide many surprises and was widely a recap of the latest data and a reminder that it is too early to declare victory on inflation and start considering policy easing.

Core inflation has come down from the peak, but two months of positive data are not enough and anyway at 4.3% year on year it remains some 2pp higher than the target. Powell stressed that 2% remains the target, and that policy will remain tight until this is achieved. Inflation on core goods and housing is trending down. Core CPI ex housing services is moving sideways on an annual base but showing a more market improvement is shorter horizons are considered (2.7% 3mth ann). This measure, according to Powell is less affected by the global disinflationary trend but responds significantly to the labour market: actually, the post-pandemic adjustment may have made it more sensitive to the unemployment rate, he reckoned.

The rebalancing in the labour market is well underway as shown by increasing participation, lower job openings, and the large drop in the workweek. Still, GDP growth was still above trend in the first half of the year (and nowcasts pointing to a strong Q3) and signs of a potential bounce in the housing market could unwind the progress on inflation, requiring further rate hikes.

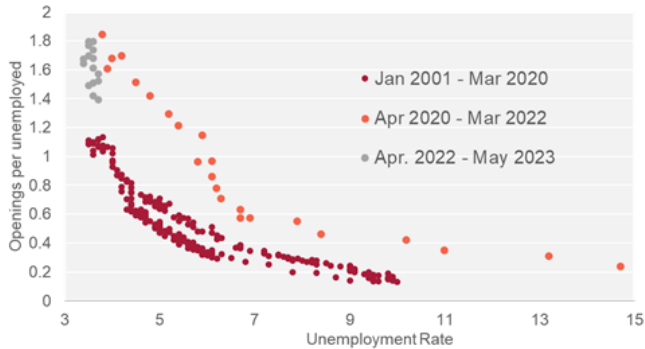
Yet, it is nearly impossible to assess in real time how tight is policy and Powell stressed again that the lags with which it impact activity and inflation are uncertain, meaning that the impact of past tightening is unlikely to have materialised in full. Therefore, in the next meetings the FOMC will assess the full range of data at its disposal and decide the next steps.

The short speech (less than 20 minutes, with no Q&A) had if anything a slightly hawkish touch, but we do not think it signals a much higher risk of further hikes. The economic data published since the July meeting do point to strong activity, but both the labour market and inflation are broadly proceeding as expected. Hawkishness was directed more at signalling again that rates will have to stay at this level for longer than market may hope.

This speech does not change our forecast for the peak rate: only very strong employment and inflation readings in August will force the Fed to hike rates in September, and by October/November we think that the increasing signs of weakening of the economy will prevent any rate rise. Yet we pushed back to the end of Q2 2024 the date of the expected first rate cut.

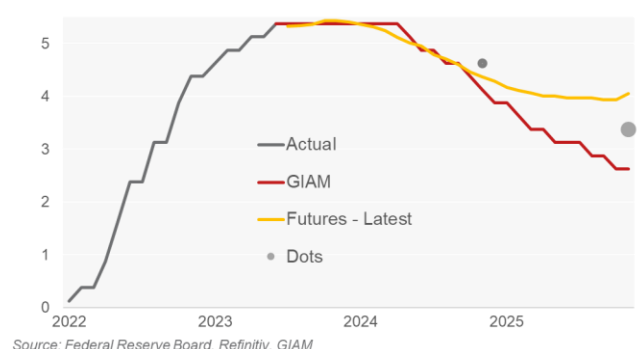
In the aftermath of the speech, markets reflected the lack of any surprise, with the yield on 10 year US treasury little changed and the S&P 500 lost marginally (0.4%)

**Labour market tightness**



Source: BLS, Refinitiv, GIAM

**Fed fund rate expectations**



Source: Federal Reserve Board, Refinitiv, GIAM

Variable	Prev. FOMC meeting	Latest	Chg.
<b>Real Activity</b>			
Weekly activity index (yoy GDP)	0.8	1.0	0.1
ISM - Manuf	47.1	46.9	-0.2
ISM - Services	51.9	50.3	-1.6
Macro Surprises	16.6	18.7	2.1
<b>Labor Market</b>			
Payroll growth (3 mth. MA)	313	253	-60
Unemp. Rate	3.5	3.7	0.2
Unemp. Rate (broad)	6.7	6.7	0.0
Hourly wages, % yoy (3 m. MA)	5.2	5.0	-0.2
<b>Prices</b>			
Core CPI	5.6	5.3	-0.3
Core PCE	4.6	4.7	0.1
Trimmed PCE	4.7	4.8	0.1
U. Mich 5 yr exp.	3.0	3.1	0.1
NY Fed 3 Y exp.	2.9	3.0	0.1
5Y5Y fwd exp.	2.2	2.3	0.0
<b>Financial Conditions</b>			
Chicago Fed index*	-0.2	-0.3	-0.1
10 yr. Treasury	3.4	3.8	0.5
- Risk neutral Component	4.0	4.4	0.4
- Term Premium	-0.7	-0.6	0.1
Yield curve (10Y - 3m)	-1.9	-1.4	0.4
S&P 500	4091	4369	6.8%
Trade Wighted Dollar	127.6	128.7	0.8%
WTI Crude Oil	68.6	69.4	1.2%

This document is based on information and opinions which Generali Insurance Asset Management S.p.A. Società di gestione del risparmio has obtained from sources within and outside of the Generali Group. While such information is believed to be reliable for the purposes used herein, no representation or warranty, expressed or implied, is made that such information or opinions are accurate or complete. The information, opinions estimates and forecasts expressed in this document are as of the date of this publication and represent only the judgment of Generali Insurance Asset Management S.p.A. Società di gestione del risparmio and may be subject to any change without notification. It shall not be considered as an explicit or implicit recommendation of investment strategy or as investment advice. Before subscribing an offer of investment services, each potential client shall be given every document provided by the regulations in force from time to time, documents to be carefully read by the client before making any investment choice. Generali Insurance Asset Management S.p.A. Società di gestione del risparmio may have taken or, and may in the future take, investment decisions for the portfolios it manages which are contrary to the views expressed herein provided. Generali Insurance Asset Management S.p.A. Società di gestione del risparmio relieves itself from any responsibility concerning mistakes or omissions and shall not be considered responsible in case of possible damages or losses related to the improper use of the information herein provided. It is recommended to look over the regulation, available on our website [www.generali-investments.com](http://www.generali-investments.com). Generali Investments is part of the Generali Group which was established in 1831 in Trieste as Assicurazioni Generali Austro Italiane. Generali Investments is a commercial brand of Generali Investments Partners S.p.A. Società di gestione del risparmio, Generali Insurance Asset Management S.p.A. Società di gestione del risparmio, Generali Investments Luxembourg S.A. and Generali Investments Holding S.p.A..

This document is based on information and opinions which Generali Insurance Asset Management S.p.A. Società di gestione del risparmio has obtained from sources within and outside of the Generali Group. While such information is believed to be reliable for the purposes used herein, no representation or warranty, expressed or implied, is made that such information or opinions are accurate or complete. The information, opinions estimates and forecasts expressed in this document are as of the date of this publication and represent only the judgment of Generali Insurance Asset Management S.p.A. Società di gestione del risparmio and may be subject to any change without notification. It shall not be considered as an explicit or implicit recommendation of investment strategy or as investment advice. Before subscribing an offer of investment services, each potential client shall be given every document provided by the regulations in force from time to time, documents to be carefully read by the client before making any investment choice. Generali Insurance Asset Management S.p.A. Società di gestione del risparmio may have taken or, and may in the future take, investment decisions for the portfolios it manages which are contrary to the views expressed herein provided. Generali Insurance Asset Management S.p. A. Società di gestione del risparmio relieves itself from any responsibility concerning mistakes or omissions and shall not be considered responsible in case of possible damages or losses related to the improper use of the information herein provided. It is recommended to look over the regulation, available on our website [www.generali-investments.com](http://www.generali-investments.com). Generali Investments is part of the Generali Group which was established in 1831 in Trieste as Assicurazioni Generali Austro Italiane. Generali Investments is a commercial brand of Generali Investments Partners S.p.A. Società di gestione del risparmio, Generali Insurance Asset Management S.p.A. Società di gestione del risparmio, Generali Investments Luxembourg S.A. and Generali Investments Holding S.p.A..