

Fed Monitor

Monitoring, not reacting to, the coronavirus

In this new publication we will give regular updates on recent Fed communications, policy signals and economic indicators. The publication includes one page of text and a few pages with relevant tables and charts. Any input on the format is much appreciated – feel free to reach out to me using my contact information in the lower right corner.

So far, the Fed has not changed its overall view on the economic outlook despite concerns over the coronavirus. Most FOMC members who have spoken since the most recent Fed meeting have said (in one way or another) that the US economy remains in good shape but that the coronavirus is a risk to the outlook (see the table on the next page containing recent quotes). **Still, it is interesting that Fed chair Powell says the Fed is ‘closely monitoring’** the coronavirus and the economic risks stemming from it, which could spill over to the US and the rest of the world. Powell said it is ‘too early’ to say what the impact on the US will be. Like the rest of us, the Fed is no expert in epidemics but stands ready to react if things worsen. **The Fed is monitoring, not reacting to, the coronavirus.**

In our view, Fed chair Powell has positioned himself as one of the more dovish members of the centrist camp. Previously, he has expressed concerns about inflation remaining below 2% and said that the labour market can tighten further, both suggesting that **a rate hike is not in the cards anytime soon and that risks are skewed towards more easing** despite the current shape of the dot plot signalling one rate hike next year. **In that respect, it is fair that investors continue to price in cuts.** Investors have priced in around 1.4 cuts this year and nearly a 50% probability of a rate cut by June. At the beginning of the year less than one cut was priced in.

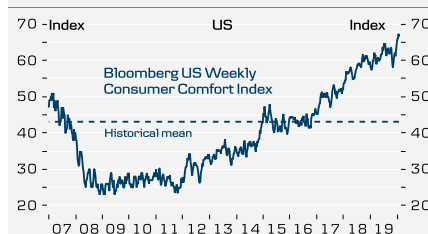
As we argued in *Research: V-shape scenario for global growth on back of coronavirus*, 3 February, **we have not changed our macro outlook for the US significantly on the back of the virus outbreak.** We believe private consumption will remain the main growth driver but that renewed uncertainty is likely to postpone a potential rebound in investments by a few months, depending on how long the uncertainty drags out. For many reasons it is difficult to compare with the SARS outbreak in 2002/03, but US private consumption growth was not affected back then. We do not have much data that has been gathered after the coronavirus outbreak, but the weekly consumer confidence indicator from Bloomberg remains at very high levels, supporting our base case. NFIB small business optimism rose in January. The jobs report for January was also strong although data was collected before the outbreak.

While we think the US is robust to the coronavirus uncertainties, we still have a slightly more pessimistic outlook on the economy than the Fed. **For now, we stick to our view that the Fed will cut rates again during the first half of 2020, probably in April, although it is not a high conviction call at this point.** We disagree with the Fed when it says that monetary policy is accommodative, as the real Fed funds rate is at the same levels as real yields (see chart page 3).

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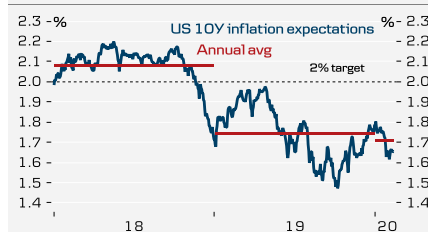
- Pages 2-3: Recent Fed quotes and Fed charts including Fed pricing
- Page 4: Macro charts

US consumer confidence not affected by coronavirus fears so far



Source: Bloomberg, Macrobond Financial, Danske Bank

US inflation expectations are low



Note: Past performance is not a reliable indicator of current or future results.

Source: Bloomberg, Federal Reserve, Macrobond Financial, Danske Bank

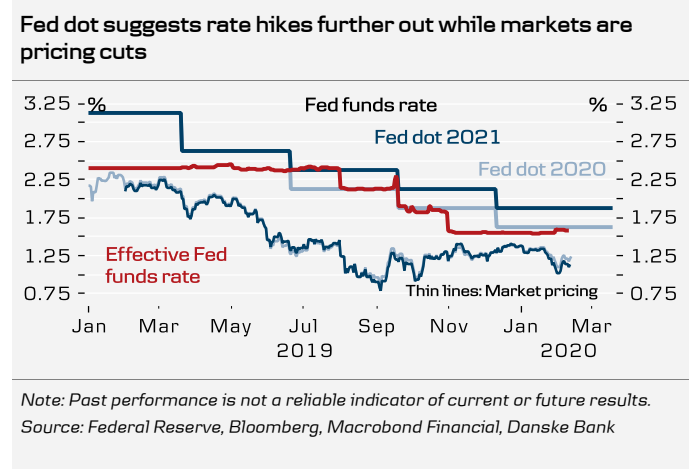
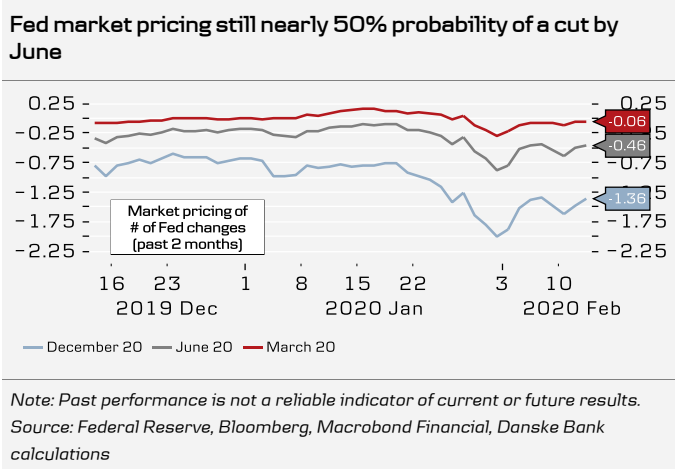
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Fed charts

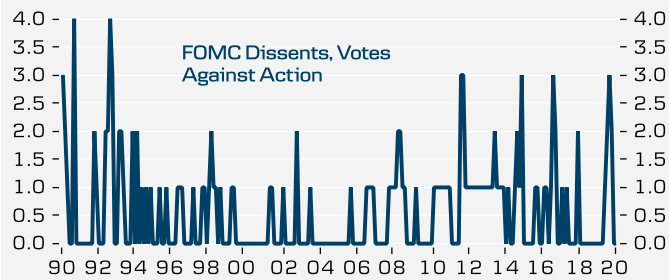
Recent Fed quotes

2020		Recent quotes	
Hawkish	George	Kansas city	
	Rosengren	Boston	
	Mester	Cleveland	
Neutral	Harker	Philadelphia	"Too early to say what impact the coronavirus will have on the global economy"
	Barkin	Richmond	
	Quarles	Board	
	Bowman (B)	Board	
	Bostic	Atlanta	"A lot of moving variables moving that make it hard to say [...] what is going to happen"
	Clarida (B)	Vice Chair	Coronavirus "is a wild card"; "looking into how it translates into the outlook"
	Williams	New York	
	Daly	San Francisco	
	Evans	Chicago	
	Powell (B)	Fed Chair	"Closely monitoring the coronavirus"; "it is too early to say"
	Brainard (B)	Board	
Kaplan	Dallas		
Dovish	Kashkari	Minneapolis	Coronavirus "clearly is a downside risk for China"; "could affect" monetary policy
	Bullard	St. Louis	Coronavirus is a "tail risk"
	Vacant	Board	
	Vacant	Board	
	Voting member	(B) Board Member	

Source: Federal Reserve, Bloomberg, Danske Bank

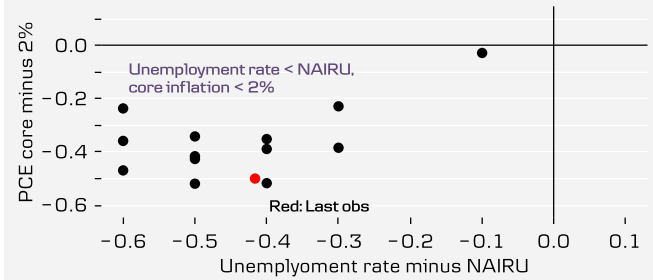


Fed prefers to work by consensus



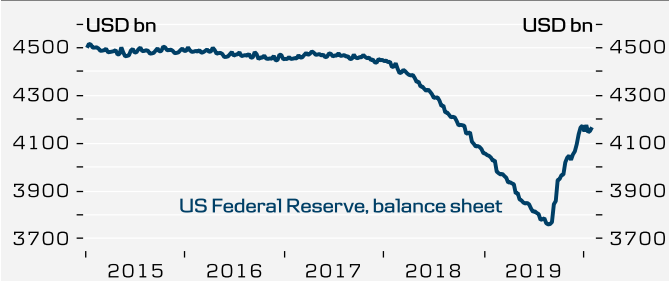
Source: St Louis Fed, Macrobond Financial, Danske Bank

Fed thinks it has fulfilled its maximum employment objective but inflation remains below 2%



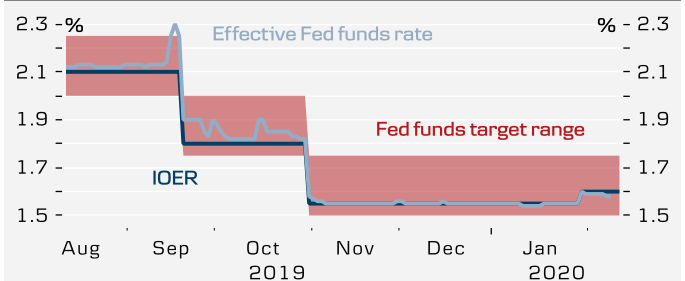
Source: Federal Reserve, BEA, BLS, Macrobond Financial, Danske Bank

Balance sheet is increasing



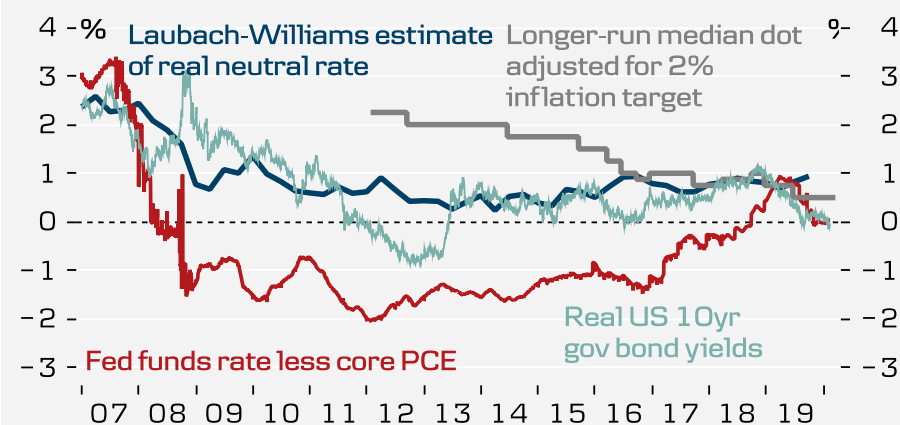
Source: Federal Reserve, Macrobond Financial, Danske Bank

Effective Fed funds rate has moved higher but remains below IOER



Note: Past performance is not a reliable indicator of current or future results. Source: Federal Reserve, Macrobond Financial, Danske Bank

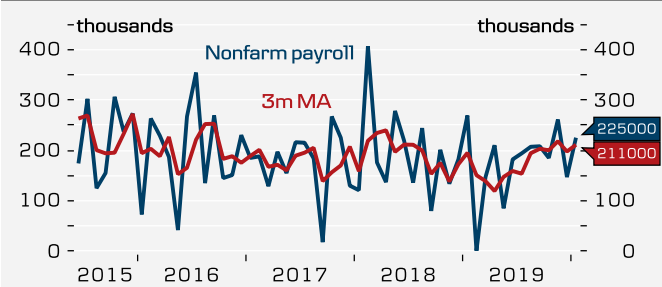
US monetary policy is not accommodative compared to market rates



Note: Past performance is not a reliable indicator of current or future results. Source: Federal Reserve, Bloomberg, NYFed, BEA, Macrobond Financial, Danske Bank

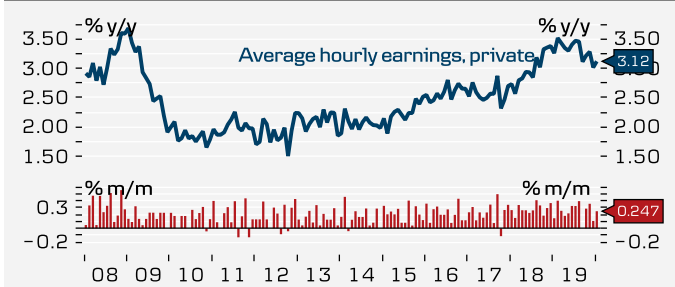
Macro charts

Employment growth is solid



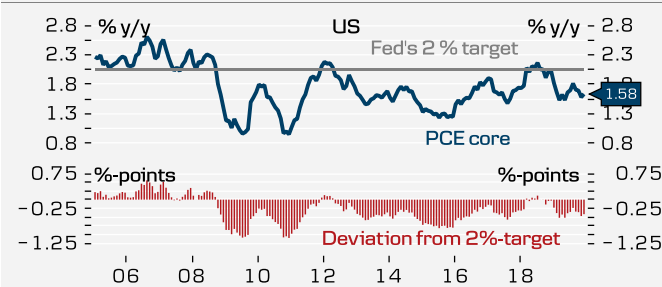
Source: BLS, Macrobond Financial, Danske Bank

Wage growth is not as high as previously but still decent



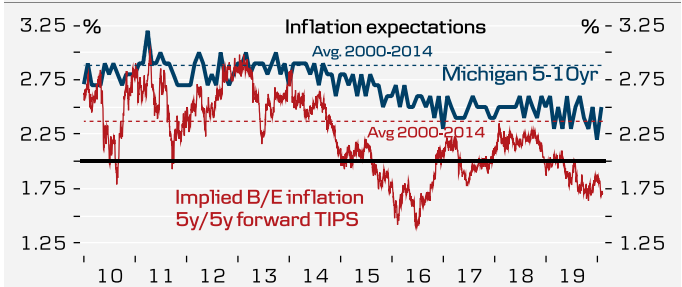
Source: BLS, Macrobond Financial, Danske Bank

PCE core inflation continues to run below the 2% target



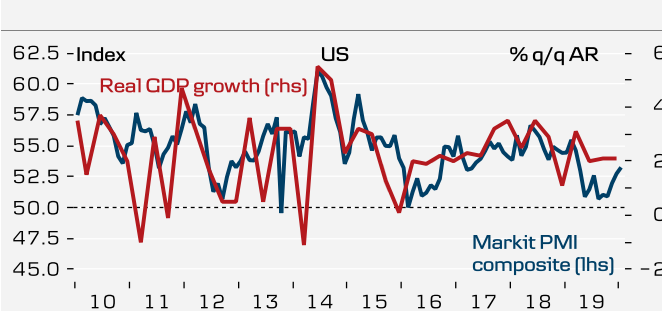
Source: BEA, Macrobond Financial, Danske Bank

Inflation expectations remain below historical average



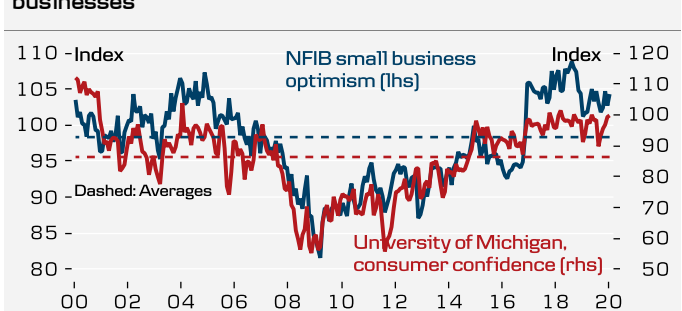
Source: Michigan, Bloomberg, Macrobond Financial, Danske Bank

Markit PMI has rebounded, signalling growth close to 2%



Source: BEA, IHS Markit, Macrobond Financial, Danske Bank

Optimism remain high among consumers and small businesses



Source: NFIB, University of Michigan, Macrobond Financial, Danske Bank

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This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of this research report is Mikael Olai Milhøj, Senior Analyst.

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Expected updates

Ad hoc.

Date of first publication

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