



MORNING BRIEFING

July 10, 2019

Fedspeak

See the [collection](#) of the individual charts linked below.

(1) From plain-vanilla Fed governor to Numero Uno. (2) Learning-by-doing. (3) The power of words. (4) Powell's, Put, Pivot, and Pirouette. (5) What does Powell mean to do next? (6) The Fed's wordsmith department. (7) "Measured" was Greenspan's favorite word. (8) Firming was needed before the Great Recession, then exceptionally low interest rates were the order of the day. (9) Defining "extended period." (10) From "gradual" to "patient" to "appropriate," and back again to what? (11) Keeping it real simple.

The Fed I: Words Have Meanings. Fed Chair Jerome Powell has been head of the Fed for a year and a half. He had been a plain-vanilla Fed governor from 5/25/12 through 2/5/18, when his four-year term as chair started. Notwithstanding his experience prior to assuming the Numero Uno role on the Federal Open Market Committee (FOMC), Powell has had lots of learning-by-doing since early last year. First and foremost, he learned that his words have meanings that can move financial markets significantly around the world:

(1) *Yesterday.* Powell's hawkish off-the-cuff comments in an [interview](#) on 10/3/18 sent stock prices reeling, resulting in a 19.8% plunge in the S&P 500 from 9/20/18 through 12/24/18 ([Fig. 1](#) and [Fig. 2](#)). Then in a 1/4/19 [panel discussion](#), he walked back his hawkish talk with dovish comments. This time, he read from a script to avoid making another bearish gaff. He said that the Fed would be "patient," implying a long pause in rate-hiking. Melissa and I dubbed it "Patient Powell's Put" in our 1/7/19 [Morning Briefing](#).

Sure enough, the stock market loved what has also been widely called "Powell's Pivot," sending the S&P 500 soaring 25.3% from the 12/24/18 low to a new record high on 4/30/19. Like the three Fed chairs before him, Powell was stress-tested by the stock market and delivered the obligatory put, just as Greenspan, Bernanke, and Yellen had done.

The escalation of the US-China trade war in early May sent stock prices down sharply again by 6.8% through 6/3/19. Once again, the Fed chair revived the market with even more dovish talk in the second paragraph of his prepared 6/4/19 [remarks](#). He said that monetary policy would "act as appropriate to sustain the expansion, with a strong labor market and inflation near our symmetric 2 percent objective," implying rate-cutting ahead. The S&P 500 soared 9.2% to yet another new record high on 7/3 thanks to "Powell's Pirouette."

(2) *Today and tomorrow.* All eyes and ears will be on Powell today and tomorrow when he testifies on monetary policy before two congressional committees. Will he pivot again back to a patient monetary policy stance following June's strong employment report? Will he reiterate that inflation is possibly being pulled down by "transitory" forces, as he said at his 5/1 [presser](#)? He hasn't mentioned that point again since. Will he walk back that notion by hinting that a rate cut might be justified by low inflation? Words certainly do have meanings. The question is what does Powell mean to do next?

As we wrote yesterday, “We wouldn’t be surprised if he made another pirouette back to a no-change stance for monetary policy. We wouldn’t be surprised if he proceeded with a 25bps cut either, but we would view it as a mistake.”

The Fed II: Word Games. Melissa and I suspect that the Fed has a wordsmith on staff. This position was most likely created by Fed Chair Alan Greenspan. The role of the wordsmith is to come up with one word or a short phrase that best describes and communicates the current monetary stance of the FOMC. That word or phrase is then repeated in the FOMC statements and minutes, and by the Fed chair and other Fed officials over and over again in their speeches and interviews. It is the monetary mantra that everyone in financial markets is expected to repeat at least on a daily basis. Below, we recap how some of the FOMC’s mantra words and phrases have been used over the years:

(1) “*Measured.*” Beginning with the [5/4/04 FOMC statement](#) under Fed Chair Alan Greenspan, the FOMC used the following phrase: “[T]he Committee believes that policy accommodation can be removed at a pace that is likely to be measured.” Those exact words remained in the statements through 11/1/05. Over this 18-month period, the federal funds rate was raised from 1.00% to 4.00% in “measured” increments of 25bps, with the first on 6/30/04 ([Fig. 3](#)).

The language around the key word was tweaked in the [12/13/05 statement](#) as follows: “The Committee judges that some further measured policy firming is likely to be needed to keep the risks to the attainment of both sustainable economic growth and price stability roughly in balance.”

(2) “*Firming may be needed.*” The word “measured” was eliminated from the FOMC’s vocabulary after that statement, but nearly the exact language around it was maintained for an additional two statements (i.e., the [1/31/06 statement](#) and [3/28/06 statement](#)): “The Committee judges that some further policy firming may be needed to keep the risks to the attainment of both sustainable economic growth and price stability roughly in balance.” By then, the federal funds rate had been raised to 4.50%. That also happened to be the first FOMC decision under Fed Chairman Ben Bernanke.

Under Bernanke’s FOMC, the [5/10/06 statement](#) similarly noted: “The Committee judges that some further policy firming may yet be needed to address inflation risks but emphasizes that the extent and timing of any such firming will depend importantly on the evolution of the economic outlook as implied by incoming information.” On the same day, the FOMC voted to raise the federal funds rate from 4.50% to 5.00%. It did so again on 8/8/06 to a peak of 5.25%, where it remained until the 9/18/07 meeting, when it was lowered to 4.75%.

The FOMC included variations of the same wording in the [6/29/06 statement](#) through the [1/31/07 statement](#): “The extent and timing of any additional firming that may be needed to address these risks will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information.”

From the 3/21/07 to the 8/7/07 meetings, the Fed was no longer in firming mode but more balanced, as suggested by the following phrase used: “Future policy adjustments will depend on the evolution of the outlook for both inflation and economic growth.” The federal funds rate remained at 5.25%.

(3) “*Will act as needed.*” There were two unscheduled statements during August 2007, in which the Fed expressed concern about the disorderly functioning of financial markets. On 9/18/07, the FOMC voted to cut the federal funds rate by 50bps, from 5.25% to 4.75%. The [statement](#) noted: “The Committee will continue to assess the effects of [financial markets] and other developments on economic prospects and will act as needed to foster price stability and sustainable economic growth.” The federal funds rate was cut again to 4.50% on 10/31/07. That language remained in the statements through 12/11/07,

when the committee announced that it was lowering the federal funds rate from 4.50% to 4.25%.

On 1/21/08, a sense of urgency to ease policy was added to the [statement](#): “Appreciable downside risks to growth remain. The Committee will continue to assess the effects of financial and other developments on economic prospects and will act in a timely manner as needed to address those risks.” With Bernanke still at the helm, growth concerns led the Fed to reduce the federal funds rate by 75bps from 4.25% to 3.50% in one shot. “Timely manner” made it into a total of three FOMC statements through 3/18/08.

“Timely manner” was dropped, and “will act as needed” remained in the [4/30/08 statement](#). By then, the Fed had lowered the federal funds rate from 3.50% to 2.00%. The FOMC took rates down further, to 1.00% on 10/29/08, just before the Fed changed its phrasing again.

(4) “*Exceptionally low levels.*” In the [12/16/08 statement](#), the Fed had established a historically low target range for the federal funds rate of 0.00%-0.25%. The economic situation had turned more desperate, as evidenced by: “The Federal Reserve will employ all available tools to promote the resumption of sustainable economic growth and to preserve price stability. In particular, the Committee anticipates that weak economic conditions are likely to warrant exceptionally low levels of the federal funds rate for some time.”

“[A]ll available tools” was changed to “a wide range of tools” in the [9/23/09 statement](#) and dropped in the [12/16/09 statement](#).

The “exceptionally low levels” phrase was attached to timeframes of “for an extended period” in the [6/22/11 statement](#), “at least through mid-2013” in the [8/9/11 statement](#), “at least through late 2014” in the [1/25/12 statement](#), and “at least through mid-2015” in the [9/13/12 statement](#). The timeframe then was extended to “as long as the unemployment rate remains above 6-1/2 percent” in the [12/12/12 statement](#).

In the [1/25/12 statement](#), the phrase “highly accommodative” joined “exceptionally low levels” to describe the policy stance. The committee stated: “To support a stronger economic recovery and to help ensure that inflation, over time, is at levels consistent with the dual mandate, the Committee expects to maintain a highly accommodative stance for monetary policy.” In other words, the Fed saw the US economy as improving but still fragile. The new phrase appeared 34 times in the statements over roughly 32 months through 9/17/14.

(5) “*Balanced approach.*” In the [1/30/13 statement](#), the Fed eliminated the use of “exceptionally low levels.” In the 12/12/12 statement just before that, “balanced approach” was added to go along with “highly accommodative.” The use of “balanced” was intended to communicate that the committee at some point would consider slowly removing policy accommodation. The statement noted: “When the Committee decides to begin to remove policy accommodation, it will take a balanced approach consistent with its longer-run goals of maximum employment and inflation of 2 percent.”

The Fed abandoned “highly accommodative” in the [10/29/14 statement](#). It was axed under Fed Chair Janet Yellen, whose first FOMC decision as Fed chair had been several months earlier on 3/19/14. However, “balanced approach” hung around through the [10/28/15 statement](#).

(6) “*Gradual.*” In the [12/16/15 statement](#), the FOMC lifted the federal funds rate to a range of 0.25%-0.50% after nearly seven years near zero. At the same time, the FOMC adopted “gradual” to describe the likely path of future policy moves, specifically: “The Committee currently expects that, with gradual adjustments in the stance of monetary policy, economic activity will continue to expand at a moderate

pace and labor market indicators will continue to strengthen.”

“Gradual” was Yellen’s last key word as Fed chair. It was passed on to Powell, who voted for the first time in his new position on 3/21/18. By then, the Fed had gradually lifted the federal funds rate to a range of 1.50%-1.75%.

(7) *“Patient.”* In early 2019, “patient” became the FOMC’s new key word in the [1/30/19 statement](#). At that point, the FOMC had raised the federal funds rate range to 2.25%-2.50% ([Fig. 4](#)). The FOMC had become increasingly concerned about persistently low inflation as well as possible further slack in the labor market and geopolitical risks, especially the US-China trade dispute. Considering this, the FOMC opted for a wait-and-see approach before making future adjustments to rates up or down. The statement noted: “In light of global economic and financial developments and muted inflation pressures, the Committee will be patient as it determines what future adjustments to the target range for the federal funds rate may be appropriate to support these outcomes.” Ironically, the word “patient” didn’t last long.

(8) *“Appropriate.”* Most recently, in the [6/19/19 statement](#), the FOMC deleted the word “patient” and emphasized “appropriate.” The statement noted: “In light of these uncertainties [to the outlook] and muted inflation pressures, the Committee will closely monitor the implications of incoming information for the economic outlook and will act as appropriate to sustain the expansion, with a strong labor market and inflation near its symmetric 2 percent objective.”

(9) *The word game.* On occasions when the Fed’s primary economic concerns, inflation and unemployment, have been tracing predictable patterns, the FOMC statement has been template-like and predictable. But when economic uncertainty has heightened or unforeseen crises like the housing collapse have hit, FOMC communication, understandably, has been less clearly focused and more haphazard.

In terms of policy today, global uncertainties like trade and its possible effects on the US economy are wildcards. So it seems that the Fed has opted for the word “appropriate” because it provides more latitude to move (or not to move) than “patient” did. But what the FOMC will do remains unpredictable in this uncertain environment.

The Fed’s word game is intended to communicate its monetary policy stance to the financial markets as simply as possible. Yet it can also create more confusion and uncertainty. In the current situation, clarity would be aided if the FOMC would simply translate “appropriate” for us: Does it mean a cut is more likely than a hike? Or does it mean the FOMC members themselves don’t have a good idea of what will happen next until the incoming data clarifies the picture?

Even better would be if the FOMC would just avoid ambiguous one-word characterizations of its stance altogether, and save markets the head-scratching. Instead, statements could just repeat *this* mantra—suitable for every occasion—over and over: “Monetary policy will continue to be data dependent.”

CALENDARS

US. Wed: Wholesale Inventories 0.4%, MBA Mortgage Applications, DOE Crude Oil Inventories, FOMC Minutes, Powell Testifies Before House Finance Services Committee, Bullard. **Thurs:** Headline & Core CPI 1.6%/2.0% y/y, Jobless Claims 221k, EIA Natural Gas Report, Powell Testifies Before Senate Banking Committee, Williams, Kashkari. (DailyFX estimates)

Global. Wed: UK GDP 03%_{m/m}/0.1%_{3m/3m}, Headline & Manufacturing Industrial Production

1.5%/1.1% y/y, China CPI & PPI 2.7%/0.3% y/y, BOC Rate Decision 1.75%. **Thurs:** Germany CPI 0.3% m/m/1.6% y/y, ECB Publishes Account of June Policy Meeting, BOE Publishes Financial Stability Report, Coeure. (DailyFX estimates)

STRATEGY INDICATORS

S&P 500 Q2 Earnings Season Monitor ([link](#)): With June quarterly results beginning to be released, just over 4% of S&P 500 companies are finished reporting revenues and earnings for Q2-2019. The y/y growth rates in revenues and earnings have slowed from Q1, but the revenue and earnings surprise metrics remain strong. Of the 22 companies in the S&P 500 that have reported through midday Tuesday, 86% exceeded industry analysts' earnings estimates. Collectively, the reporters have averaged a y/y earnings decline of 11.0%, and exceeded forecasts by an average of 6.0%. On the revenue side, 77% of companies beat their Q2 sales estimates so far, with results coming in 0.9% above forecast and 2.9% higher than a year earlier. Q2 earnings growth results are positive y/y for 64% of companies, vs a higher 69% at the same point in Q1, but Q2 revenues have risen y/y for 86% vs a lower 76% during Q1. These figures will change markedly as more Q2-2019 results are reported in the coming weeks. Looking at earnings during the same point in the Q1-2018 reporting period, a lower percentage of companies (81%) in the S&P 500 had beaten consensus earnings estimates by a lower 5.5%, but earnings were up a higher 4.3% y/y. With respect to revenues at this point in the Q1 season, a lower 45% had exceeded revenue forecasts by a lower 0.5%, but sales rose a greater 4.0% y/y. The early results for Q2 indicate a continuation of the marked slowdown in revenue and earnings growth compared to 2018, but that comes as no surprise to investors. Q1-2019 was the 11th straight quarter of positive y/y earnings growth and the 12th of positive revenue growth. However, earnings growth trailed revenue growth during Q1-2019 for the first time since Q2-2016, which has happened just five times in the 42 quarters since the bull market started in Q1-2009; it's likely to happen for a sixth time in Q2-2019.

US ECONOMIC INDICATORS

JOLTS ([link](#)): Job openings in May fell for the third time in four months, though were still within 303,000 of November's record-high reading of 7.626 million. Openings fell 49,000 in May and 302,000 over the four-month period to 7.323 million. May's ratio of unemployed workers per job opening was below 1.00 for the 15th straight month, at 0.80, with job openings exceeding unemployed workers by 1.4 million. Hirings in May sank 266,000 to 5.725 million, while total separations dropped 192,000 to 5.495 million—after reaching record highs of 5.991 million and 5.687 million, respectively, in April. The latest hiring and separations data yielded an employment advance of 230,000 in May, 158,000 above May's payroll gain of 72,000—overstating the increase for the sixth time in seven months. Those quitting their jobs fell 91,000 to 3.425 million, after rising four of the prior five months, by a total of 137,000, to a record-high 3.516 million. May's private-industry job openings (4.9%) rate held just below its record rate of 5.2% posted in October and November, while the quit (2.5) rate held just below its cyclical high of 2.6%—bouncing between 2.5% and 2.6% since mid-2018. The hires rate ticked down to 4.2%, fluctuating in a flat trend from 4.2% and 4.4% since reaching a cyclical high of 4.4% last May.

NFIB Small Business Optimism Index ([link](#)): "Last month, small business owners curbed spending, sales expectations and profits both fell, and the outlook for expansion dampened. When you add difficulty finding qualified workers and harmful state level laws and regulations, you're left with a volatile mix where uncertainty has increased to levels not seen in more than two years," said NFIB President and CEO Juanita D. Duggan. The Small Business Optimism Index (SBOI) fell in June for the first time since the start of the year—to 103.3—after rising from 101.2 in January (which was the lowest reading since November 2016) to 105.0 in May; it was at a record high of 108.8 last August. In June, six components deteriorated, three improved, while the business conditions (16%) component was

unchanged. The Uncertainty Index (to 87 from 79) rose substantially, to its highest level since March 2017, as 30% of owners reported that recent changes in China trade policy has negatively impacted their business. Meanwhile, the biggest drags on June's SBOI were sales expectations (to 17% from 23%), earnings trends (-7 from -1), and the environment for expansion (24 from 30), followed by capital spending plans (26 from 30), hiring plans (19 from 21), and current job openings (36 from 38). Partially offsetting these declines were improvements in current inventory (0 from -4), expected credit conditions (-3 from -5), and plans to increase inventories (3 from 2). Despite the recent setback, Duggan noted: "The economy is still advancing at a solid pace, but it is expected to be a slower pace than the first quarter."

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