Opinion | 3 May 2018

FOMC meeting leaves little for stock bulls

Nothing in the FOMC statement suggests that rates will not be raised further in coming quarters, or that inflation will be allowed to run hot

Source: Federal Reserve

Inflation - core and headline, at target - more rate rises coming

"The FOMC could not have been clearer in its statement yesterday. Inflation, whichever way you look at it, is no barrier to further rate rises. But with inflation expectations remaining subdued, there is no need for the Fed to speed up its pace of tightening either. The key sentences are "...both overall inflation and inflation for items other than food and energy have moved close to 2 percent. Market-based measures of inflation compensation remain low; survey-based measures of longer-term inflation expectations are little changed, on balance."

The full FOMC statement is available here.

That wasn't enough to get 10Y US Treasury yields over the 3% hurdle, and it provided little comfort for stock bulls, as equities fell, though they remain some distance from levels that would suggest a bigger correction was imminent. The USD was not hurt by the move, and continues to make gains against the EUR, despite some comments by Jens Weidemann about the timing of rate hikes next year - you're not the ECB President yet Jens!

Some market pundits suggest the equity sell-off was on hints that the FOMC might be prepared to let inflation run a little hot. That is bunkum. Not only is there no suggestion of an asymmetric approach to inflation in this statement, if that really were the case, then stocks, which are a nominal, not real asset, should rally and bond yields would have shot higher. Neither happened because "running hot" hypothesis is entirely unsupported by the facts today. That could yet change. And don't forget the US jobs report tomorrow - especially wages, which could push the inflation story again.

Mnuchin et al are in China - but for how long?

We wrote earlier this week about the US mission to China to strike a deal on trade and avert a trade war. Well, they are on the ground now, though the mood music coming out isn't great. It sounds like they have flexible plane tickets, as they continue to stress that they will return early if they do not think there is much promise of progress. Watch the wires for hints of the direction this is going, This could be a market mover in either direction. But more likely down.

No respite for PM May, or the GBP as Lord's votes amendment on Brexit bill

UK sterling remains under downward pressure against even a falling EUR, with the Brexit woes of PM Theresa May piling up around her. Last night's amendment on ensuring no physical restrictions at the Irish border with Northern Ireland, marks the tenth defeat in the House of Lords. And though a spokesman for the PM suggested that the amendments would be stripped out of the Brexit legislation, it is not clear that May has the support necessary in the Commons to enable her to do so. The only way out currently is for a type of "hard border" mid-way across the Irish Sea, if Northern Ireland is kept within a customs union and possibly the single market. Its hard to see how the UK could accept that. Accepting a Customs Union for the whole of the UK is another option that could sort this, but that would remove most of the point of Brexit for those who want to leave the EU. Difficult for the PM, difficult for the GBP. Answers needed soon or the UK could find itself leaving the EU without a deal. One wonders if some of the less economically and financially literate members of the UK cabinet secretly want this...