

What Will the Fed Do Next?

By: [Sawyer Rothmann](#)

What will the Fed do? This is the question that every Financial Advisor has found themselves asking more frequently this past year. A question that, given the correct answer, is the holy grail to investing for the foreseeable future. A question people all around the world are trying to take educated guesses on in pieces that, when printed out, are thicker than the Accounting Desk Book or your child's Harry Potter book collection.

What has the Fed done?

A question more easily answered, which is exactly what I will do in less than 1000 words.

The Fed had their November meeting last week where they discussed the current state of the economy, inflation, the jobs market, and everything in between. As the Fed does after every periodic meeting, they released a statement shortly before Fed Chair Powell held a press conference. Markets perceived the initial statement as leaning “dovish,” or pointing towards a pivot away from their current pace of rate hikes, due to some new commentary around the Fed accounting for cumulative tightening of policy, the lags that come with that tightening, and ongoing economic and financial developments.

Once the conference began, however, Powell's commentary slowly became more and more adjacent to what we've heard in the past few meetings as things took a turn to what many investors have deemed “hawkish,” or pointing towards continued monetary tightening. It was eventually clear there would be no pause or substantial slowdown (i.e. less than 50bps) in hikes this year as Powell hinted that the terminal rate may be higher than previously expected.

Chair Powell began his speech with the same boiler plate language he has for the past few meetings:

- » “My colleagues and I are strongly committed to bringing inflation back down to our 2% goal...”
- » “Price stability is the responsibility of the Federal Reserve, and serves as the bedrock of our economy...”
- » “Longer term inflation expectations remain well anchored, but that is not grounds for complacency...”

What is the terminal rate?

The terminal rate is the rate that is viewed as the peak where benchmark interest rates will come to rest before the Fed begins trimming back. In a perfect world, it would be the rate where the Fed is comfortable sitting at while they watch inflation cool down before any possible turmoil hits the economy or jobs market. Prior to this Fed meeting, many believed that rate to be slightly under 5%. Now we may have eclipsed that number.

Powell then took a dovish turn by saying, “Decisive evidence of slowing inflation is not the bar for slowing the pace of rate increases.” He continued on by explaining, “The time to downshift to a slower pace of hikes may come as soon as next meeting, or the one after that.” This was all investors needed to begin licking their wounds from his extended terminal rate commentary.

Is inflation is becoming entrenched?

When asked if inflation is becoming entrenched, Powell explained that short term expectations of inflation rising may work their way into wages eventually, but that long term expectations of inflation show stability. Ultimately, he concluded that there is no scientific way to assess if inflation is becoming entrenched.

What exactly is entrenched inflation and why is it such a bad thing? Inflation becomes entrenched as it works its way into the balance sheets of businesses around the country. As the things we buy begin to cost more, people need more income to purchase them. So those people naturally ask their employer for higher wages. Those wages are now an inflated cost on their employer's income statement. As the things the employer wants to buy or invest in begin to cost more, they need more money for expenses. So, the employer will charge their customers to pay more for those inflated costs. Now, if they can successfully do that is a discussion for another piece. And that dynamic has the potential to build on itself in an endless circle, short-circuiting only in the event that there is a change in the balance of supply and demand. But this again is a conversation for another time.

What about monetary policy?

Powell went on to speak about his thoughts around the lag of monetary policy and how the Fed looks at it. He explained that old theories say monetary policy acts with long and variable lags, but new literature suggests financial conditions act well before monetary policy decisions. This makes sense to the 21st century investor – America is more interconnected and data-driven than ever. Expectations of what might happen have just as much impact as what actually does happen. And so, it's highly uncertain how quickly the economy adjusts to financial tightening, but at least the Fed acknowledges they are aware of the dynamics.

The market ultimately came down by the end of the press conference after Powell struck another hawkish tone, saying “It's very premature to be thinking about pausing hikes, we have ways to go.”

So, what will the Fed do next?

The market seems to think a 50 basis point hike is the likely result for the next December Fed meeting. We have two CPI prints between now and then which will likely weigh heavily on their ultimate decision. We can't tell you with 100% certainty what they will do, but we can watch the data and react appropriately as rational investors.

Cerity Partners LLC (“Cerity Partners”) is an SEC-registered investment adviser with office locations throughout the United States. Registration of an Investment Advisor does not imply any level of skill or training. The foregoing is limited to general information about Cerity Partners' financial market outlook. You should not construe the information contained herein as personalized investment, tax, or legal advice. There is no guarantee that the views and opinions expressed in this commentary will come to pass. The information presented is subject to change without notice and should not be considered as an offer to sell or a solicitation of an offer to buy any security. Material economic conditions and/or events may affect future results. All information is deemed reliable as of the date of this commentary but is not guaranteed. Before making any decision or taking any action that may affect your finances or your company's finances, you should consult a qualified professional adviser. For information pertaining to the registration status of Cerity Partners, please contact us or refer to the Investment Adviser Public Disclosure website (www.adviserinfo.sec.gov). For additional information about Cerity Partners, including fees, conflicts of interest, and services, send for our disclosure statement as set forth on Form CRS and ADV Part 2 using the contact information herein. Please read the disclosure statement carefully before you invest or send money.

Indices or other financial benchmarks are provided for illustration purposes only. Indices are unmanaged, statistical composites and an individual cannot directly invest in an index. Any returns portrayed do not reflect the deduction of underlying investment expenses and third-party fees to purchase the securities they represent. Past performance is no guarantee of future results. Data from indices (i.e., the S&P 500) are supplied by third party suppliers. Cerity Partners does not attest to the accuracy or reliability of these numbers nor the methods of calculation from which they are derived. Investing in the financial markets involves risk, including the loss of the principal amount invested; and may not be appropriate for everyone.

Certain information contained herein concerning economic trends and market performance trends are based on or derived from information provided by independent third-party sources that, in certain cases, may not have been updated through the date of this information. While such information is believed to be reliable for the purposes used herein, Cerity Partners has not independently verified the assumptions on which such information is based nor assumes any responsibility for the accuracy or completeness of such information.

ceritypartners.com/contact

©2022 Cerity Partners LLC, an SEC-registered investment adviser. All Rights Reserved.

(11/22)