FED WATCH: THE FINAL COUNTDOWN

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For all intents and purposes, the pause at the June FOMC meeting just turned into a skip, as the Fed came back with another quarter-point rate hike at the July policy convocation. This pushes the new Fed Funds target range to 5.25%–5.50%, the highest level since early 2001. Investors are now left to ponder if Powell & Co. are finally finished with this rate hike cycle or if there is another move waiting in the wings.

If you believe the Fed's dot plot, it appears the voting members have one more rate increase in store for 2023. Indeed, their median estimate for Fed Funds was updated last month to show a 5.60% reading, or 50 basis points (bps) above the prior estimate from March. I've blogged before about the reliability of these dot plots, so the markets could be excused if they are not 100% on-board with this outlook at the current time. That being said, we have witnessed over the last month or so how the Treasury arena has finally come around to being more in line with Fed messaging.

That brings us back to the July FOMC meeting and why the Fed did not raise rates in June. Yes, it is a moot point now, but I still can't understand what changed so much to cause them to implement this most recent rate hike rather than just raising the Fed Funds target six weeks ago and avoiding the somewhat confusing signals that have occurred over this interim period.

The more important question now is what investors should be expecting for U.S. monetary policy for the remainder of this year. From the FOMC's perspective, the Fed will continue to weigh the full impact of the now 525 bps in rate hikes that have already occurred in conjunction with the expected further tightening in credit conditions from the regional banking fallout. Thus, the policy makers remain in full "data dependent" mode. It is also important to remember that another key part of the Fed's tightening process, quantitative tightening (QT), continues unabated.

Based on various reports, Powell was supposedly not a fan of the "stop and go" approach to policy decisions. However, the July rate hike seemingly puts that notion to rest. This places the September FOMC meeting now in focus. This policy gathering could prove to be an integral part of the money and bond market landscape as we enter Q4 and head into the early portion of 2024.

The Bottom Line

Whether or not another rate increase is in the cards for this year, it does seem as if the Fed is now either at, or close to, the end of this rate hike cycle. In addition, rate cuts have now been completely taken off the table until perhaps later in the first quarter of next year. In other words, investors should focus on rates more likely being "higher for longer" in their portfolio decision-making process.

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Federal Open Market Committee (FOMC) : The branch of the Federal Reserve Board that determines the direction of monetary policy.

Rate Hike : refers to an increase in the policy rate set by a central bank. In the U.S., this generally refers to the Federal Funds Target Rate.

Quantitative Tightening : Quantitative easing is a process whereby a central bank targets lowering longer-term interest rates by purchasing bonds and other securities to stimulate the economy. Quantitative tightening is the reverse process whereby securities are either sold or the proceeds of maturing securities are not reinvested with the goal of tightening economic conditions to prevent the economy from overheating.