

January 10, 2019

## A Confident Powell Essentially Takes March Off the Table

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In a talk today, Powell reiterated that he was quite confident in the U.S. economic outlook. He downplayed a number of factors that have preoccupied markets, to a surprising extent in some cases. However, he was confident without conveying a hawkish signal. When Powell was asked specifically about the prospect of hike in the near term, he emphasized the FOMC's ability to be "patient," given the muted inflation outlook: "You should anticipate that we're going to be patient, and watching, and waiting, and seeing." He said that he wanted to see the data confirm that the economy is on track in 2019 after a strong 2018. This response suggests that the FOMC will pause rate hikes at least through March, as this is a difficult condition to fulfill in just a couple more months. At the March meeting, while Powell may continue to be quite confident that the economy remains on track, he simply won't have enough data in hand for 2019 to confirm that. Downside risks call for a risk management approach, which, in turn, calls for a pause in March. This reinforces our decision to drop our baseline of a March hike.

Powell's comments were at least as positive as we would have expected on virtually every aspect of the outlook. He saw nothing to suggest that there was an elevated risk of recession in the near term. The U.S. data show no sign of a slowdown, and he thinks the U.S. economy has strong momentum. The concern stems from a slowing in foreign economies, particularly the EU and China, which does have a negative effect on the U.S. outlook. He elaborated more on recent developments in the Chinese economic data than we would have expected, and he was relatively optimistic. He said there is clearly a slowing, but that he doesn't see a reason to expect anything less "another year of solid growth." He commented that tariffs don't seem to be having a significant impact on either the U.S. economy or the Chinese economy. On Brexit, he expressed little concern, saying that the Fed was prepared for the full range of outcomes. As a base case, he expected some effect on the U.K. and E.U. Powell didn't express any unusual concern about the shutdown, pointing to the fact that they have typically been short and had little impact, but he did warn that, "A longer shutdown is something we haven't had. If we had an extended shutdown then I do think that would show up in the data pretty clearly." He also pointed out that the shutdown affects economy policymaking by halting the publication of some economic data.

Powell did stir markets with his comments on balance sheet normalization. Markets have been speculating about the prospect of the Fed altering its balance sheet normalization plans, something that FOMC participants discussed at the December 2018 FOMC meeting, according to the minutes. But Powell suggested that the FOMC intends to allow the balance sheet to shrink much further, saying that "It will be substantially smaller than it is now." He provided no hint that any adjustment to the reinvestment policy would be considered in the near term.

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[Powell Remarks: More Dovish, Balance Sheet Included](#)

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