Weekly Commentary

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Fed sporting blinders

The Federal Reserve has been contrarian lately. It raised rates at its March Federal Open Market Committee (FOMC) meeting in spite of stress in the bank sector. Then it didn't increase them in June despite brinkmanship in Congress over the raising of the U.S. debt limit. And that "pause" had a contradiction of sorts, as policymakers projected they will raise the target range, currently at 5-5.25%, at least one more time.

That takes us to the next FOMC meeting, ending July 26. With those projections and hawkish Fed Speak in recent weeks, it would seem another hike is on the way. Probably a 25 basis-point variety. But the Consumer Price Index (CPI) for June, released last week, showed inflation has continued to fall. Headline CPI is now 3% year-over-year. That's close to the 2% level the Fed has said it targets. But it pays more attention to core CPI (which strips out volatile food and energy prices), and while that has also declined, at 4.8% it is still high for policymakers' liking. Plus, they also factor in other measures of inflation, most notably the Personal Consumption Expenditures Index, which is still elevated.

So, we think it likely the Fed will raise rates despite the good news about headline CPI. This Fed has made clear too many times it is determined to crush inflation to doubt it now.

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