

Sarasin Six Minute Strategy

A quiet revolution at the Federal Reserve...?

August 2020



The Fed's Policy review...

Jerome H. Powell – Jackson Hole, Wyoming (via Webcast)



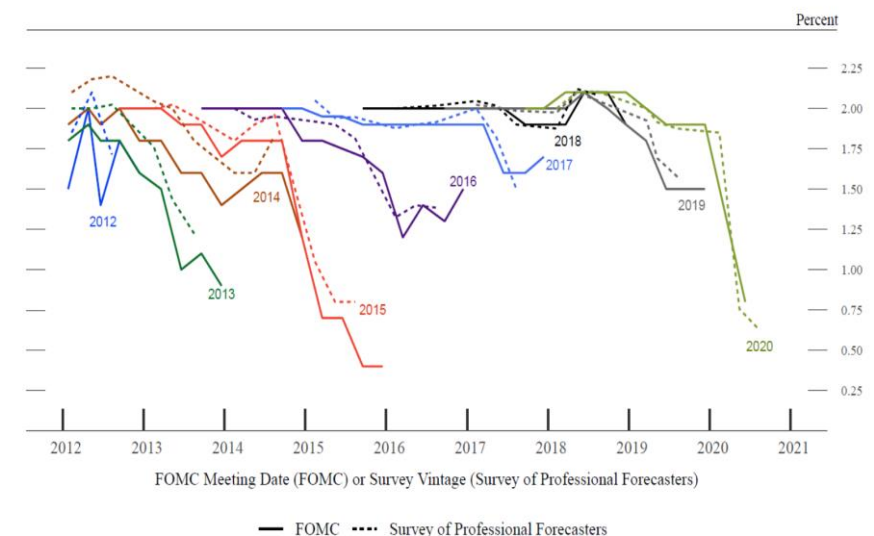
Four Economic Developments motivated this 2019 review:



Persistent undershooting of inflation

1. The long-run growth rate of US GDP has declined
2. The general level of interest rates has fallen in the US and around the world
3. Until earlier this year the recent expansion saw the best labour market years, with gains shared more widely across society.
4. This historically strong labour market *did not trigger* a significant rise in inflation.

Figure 3: Evolution of Real-Time Projections for Personal Consumption Expenditures Inflation



Note: The Federal Open Market Committee (FOMC) data, represented by the solid lines, are median projections published quarterly; the latest data vintage is June 2020. For 2015:Q1 and 2015:Q2, the data are central tendency midpoints. The Survey of Professional Forecasters (SPF) data, represented by the dashed lines, are median projections published quarterly; the latest data vintage corresponds to 2020:Q3.

Source: For FOMC, Summary of Economic Projections, available on the Board's website at <https://www.federalreserve.gov/monetarypolicy/fomccalendars.htm>; for SPF, Federal Reserve Bank of Philadelphia.

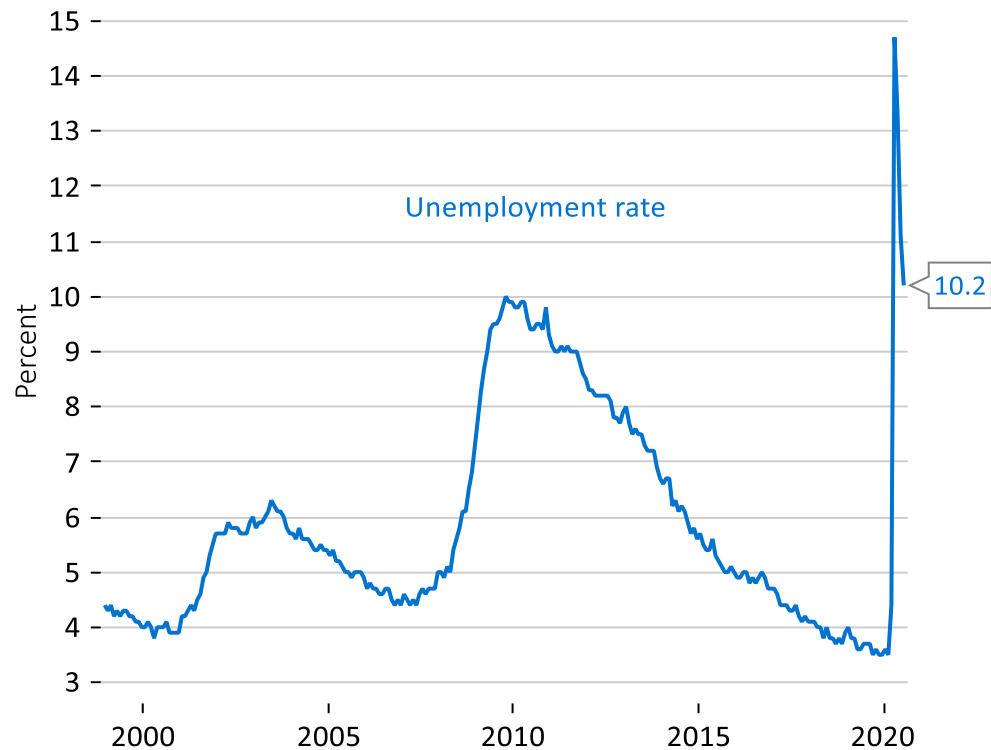
Source: Federal Reserve/Jackson Hole 27 8 2020

Fed Policy Review:

New framework to emphasise full employment and target average inflation

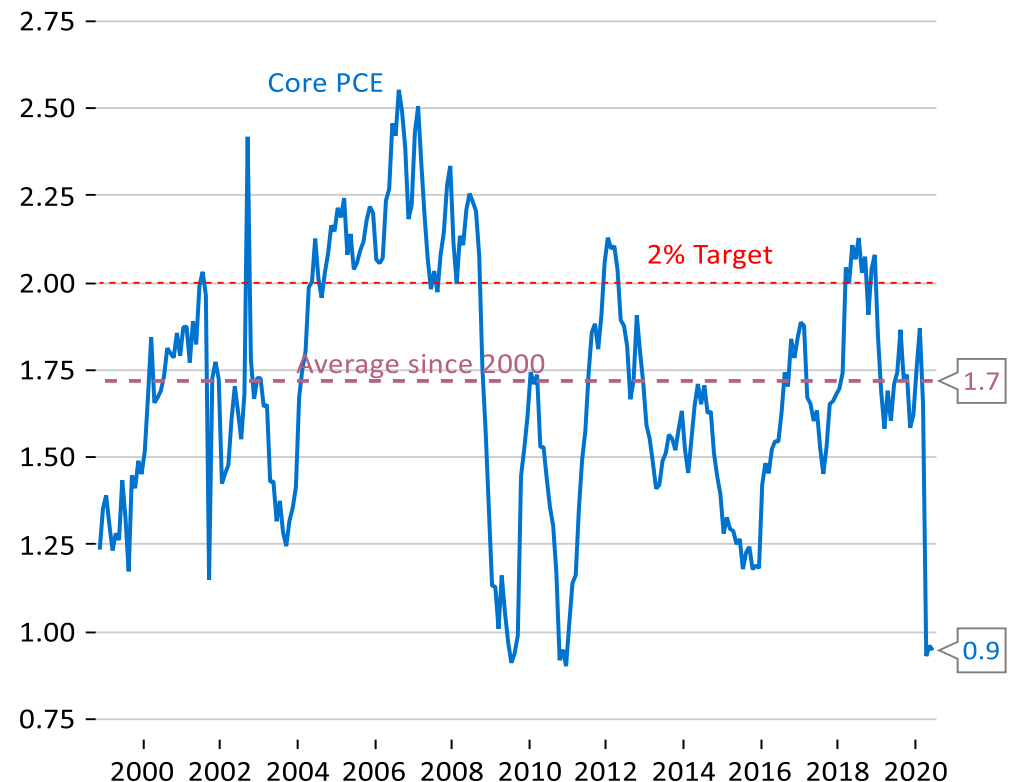
Shortfalls of employment from its maximum level

Unemployment rate



Source: Macrobond, 27.08.20

Inflation – Core Personal Consumption expenditure deflator



Source: Macrobond, 28.08.20

New Fed Statement

Summary



Price Stability

- “In order to anchor longer-term inflation expectations at this level, the Committee seeks to achieve inflation that averages 2 percent over time.”
- “Our decisions about appropriate monetary policy will continue to reflect a broad array of considerations and will not be dictated by any formula.”

Employment

- Fed Policy informed by “assessments of the shortfalls of employment from its maximum level” rather than by “deviations from its maximum level” as in the previous statement
- “Maximum employment is a broad based and inclusive goal” with particular benefits for “low & moderate income communities.”

Our Conclusions

- Dovish – a higher tolerance for inflation but how relevant for now?
- Significant – Early, forceful, pragmatic (flexible inflation targeting)
- Inclusive employment goal – a welcome but quiet revolution

Source: Federal Reserve/Jackson Hole 27.08.20

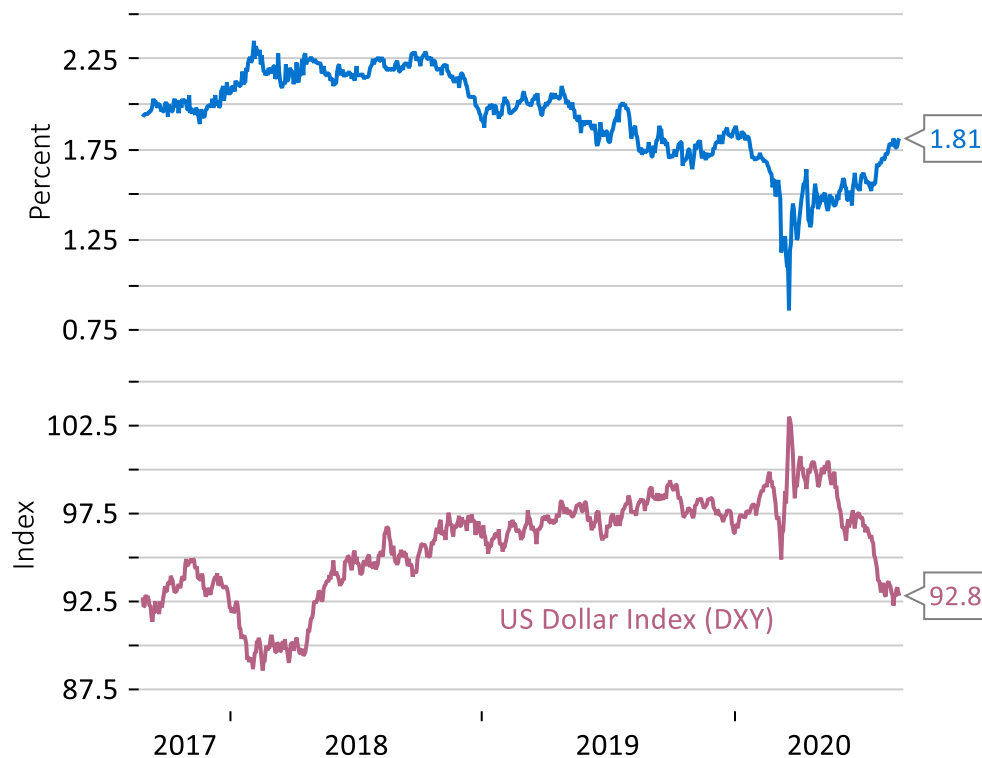
Market Reaction:

US inflation expectations tick up, Dollar lower, bond curve steepens...



US inflation expectations climbing as dollar falls...

US Inflation Expectation Rate, 5 Year 5 Year Forward



Source: Macrobond, 27.08.20



Modest rise in US bond yields this month...

US 10 Year T -Bond



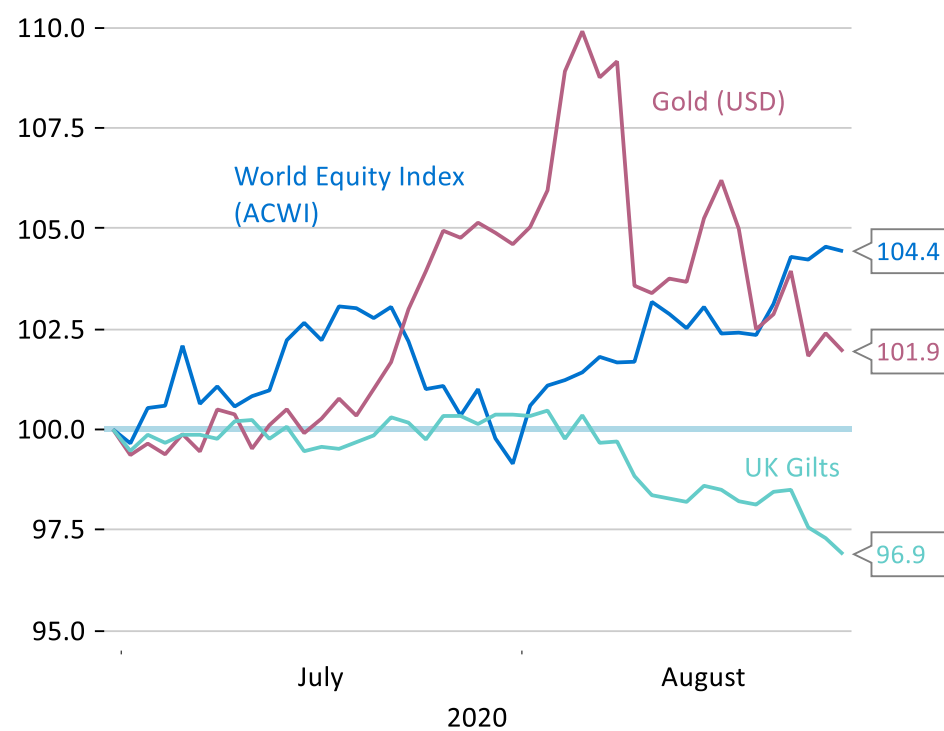
Source: Macrobond, 27.08.20

Market Performance H2 2020 to date



Asset Returns (Sterling Investor)

Global Asset Class Returns H2 2020 (GBP)



Source: Macrobond, 28.08.20



Could this signal a move up in bond market volatility?

US Bond Volatility Index (MOVE 1m)



Source: Macrobond, 28.08.20

Could this be the beginning of a change in equity leadership...?



Market 'Heavyweights' dominate again

US S&P500 Indices

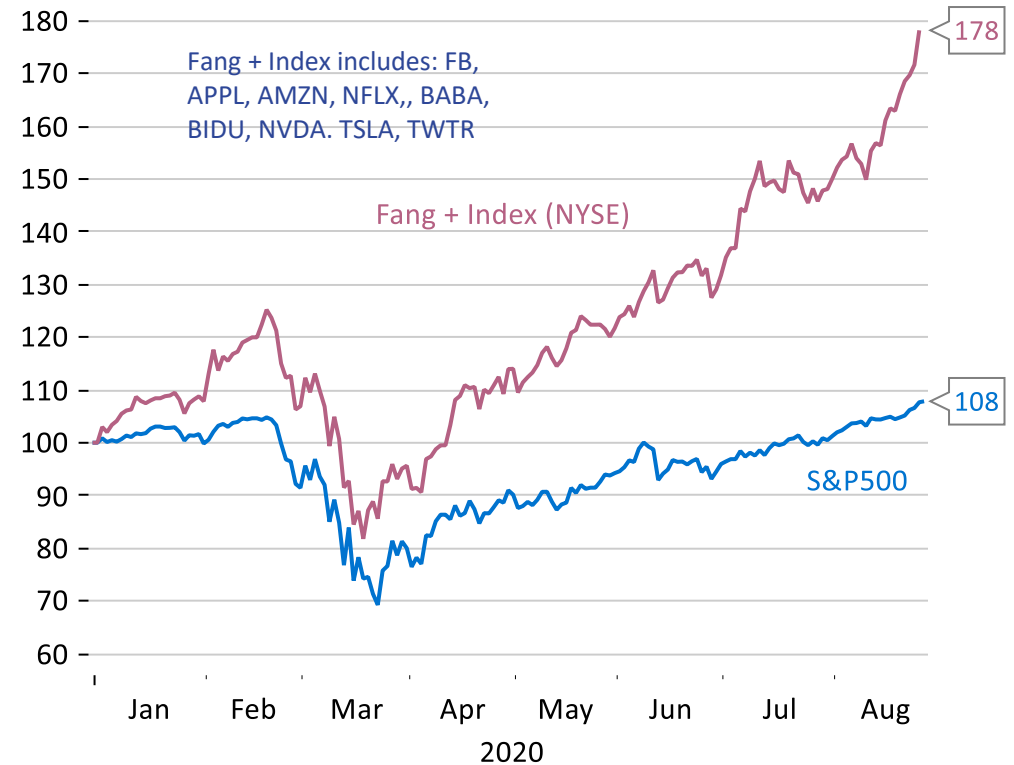


Source: Macrobond, 24.08.20



FAANGs surge on strong earnings & post COVID economy

US S&P500 Indices



Source: Macrobond, 27.08.20

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