

# FED WATCH: "BLUES CLUES"

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Well, here we are at the "halftime report" for the [Federal Reserve \(Fed\)](#). What do I mean by that, you might ask? The Fed just wrapped up its fourth [FOMC](#) meeting for 2021 and has four more remaining. (Plus, it is mid-June after all.) Thus far, from a broader policy perspective, the voting members are at the midway point for 2021, and they are still in "steady as she goes" mode in terms of their current policy setting. However, we seem to be getting closer to the beginning of the Fed initiating an "exit strategy" of sorts.

So, what are the takeaways from this policy convocation? Primarily, the Fed is still apparently in no hurry to remove its unprecedented accommodation, BUT some members do seem to be ready to put a timeline of sorts together to move slowly in that direction. In fact, the language being used in a variety of different forums has been "talking about, talking about [tapering](#)."

This meeting carried the "trifecta": a policy statement, Powell presser and the Summary of Economic Projections (SEP). In no surprise, the voting members "marked to market" their policy statement, as well as the SEP, to reflect the incoming data that had been received. There's no doubt the broader economic numbers have been pointing to another outsized gain for real [GDP](#) in Q2. However, sprinkled in has been the highly publicized spike in [inflation](#) juxtaposed against the disappointing (in relative terms) employment numbers. While acknowledging the inflation story of late, the "transitory" stance still holds sway. From the Fed's point of view, the aforementioned employment data seems to be carrying the most weight, underscoring Powell's cautious approach.

Heading into the June FOMC meeting, I recently blogged (and podcasted) that I'd be watching the Fed's "[blue dots](#)," [aka its Fed Funds estimates](#). From December through March, the number of members pushing up the timing of the Fed's median forecast of a 2024 first rate hike had been increasing modestly. However, this time around a more notable change did take place, as the number of Fed officials pushing up the first rate hike to 2023 outnumbered the "2024" crowd. These "blue dots" will more than likely be a fluid situation for the remainder of this year, as the Fed increasingly becomes data dependent.

## Conclusion

For fixed income investors, the recent trading activity in the [U.S. Treasury \(UST\) 10-Year yield](#) underscores how the market has already "priced in" the current [macro](#)/Fed policy setting. For the second half of the year, I would argue the UST market will be taking its cue from any potential shifts in the Fed's thinking, namely the discussion surrounding tapering and the exit strategy in more broader terms. Remember, the policy makers recently announced, without much fanfare, they would be winding down their holdings of corporate bonds on their [balance sheet](#). Technically speaking, the exit strategy has begun.

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## DEFINITIONS

**Federal Reserve** : The Federal Reserve System is the central banking system of the United States.

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

**Tapering** : A shift in monetary policy by which the Federal Reserve would begin decreasing the amount of bonds it purchases.

**Gross domestic product (GDP)** : The sum total of all goods and services produced across an economy.

**Inflation** : Characterized by rising price levels.

**Blue dots** : the midpoint target range/level of the FOMC participants' projections for the future Federal Funds Rate.

**10- Year Treasury** : a debt obligation of the U.S. government with an original maturity of ten years.

**Macro** : Focused on issues impacting the overall economic landscape as opposed to those only impacting individual companies.

**Balance sheet** : refers to the cash and cash equivalents part of the Current Assets on a firms balance sheet and cash available for purchasing new position.