Powell’s most pressing job is going to be both in getting key Fed officials all on the same page, and then effectively and consistently communicating that message to an increasingly conflicted and nervous constituency. (ddp)

Mixed missions, mixed messages

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Recent developments suggest that the role of Federal Reserve chair is not likely to become any less demanding in the weeks and months ahead.

Not only does the head of the US central bank bear the awesome responsibility of optimizing growth in the world’s largest and most complex economy, but that person also plays a leading role in setting the tone for monetary policy globally while also being tasked as primary guardian of financial market stability.

This is a challenging enough undertaking under a more normal set of conditions, but precious little about the current economic environment could be categorized as normal. Keep in mind that GDP growth during this expansion is averaging only about half the pace of prior recoveries, and inflation still falls short of the Fed’s 2% target despite the tightest labor market conditions in a generation. To make matters worse, trade tensions have risen to levels rarely seen since the Bretton Woods accord, with escalating tariffs, export restrictions, and even the potential "weaponization" of monetary policy.

This sense of "mission conflict" is also reflected by the level of dissension that currently exists within the ranks of the Fed. At their most recent meeting back on 31 July, the Federal Open Market Committee (FOMC) opted to lower the target federal funds rate by 25 basis points, as expected. Yet the views of the committee with regards to the rationale behind that differed widely—as did the opinions over the efficacy of the rate cut. While some saw the move as a response to a slowing of global growth, others viewed this as a risk-management measure to guard against further deceleration, while still others categorized the cut as a response to low inflation expectations. And although two members of the FOMC voted against the measure and were supportive of holding rates steady, comments from others suggest they would have preferred the Fed to move even more aggressively in easing policy.

In the meantime, President Donald Trump has continued to ratchet up his own criticism of the Fed for what he describes as a “horrendous lack of vision.” In his most recent response to the announcement of China’s retaliatory trade measures, President Trump once again took a direct shot at Jay Powell by pondering whether the Fed chair was a “bigger enemy” to the US than Chinese President Xi Jinping. So it’s clear that the president instead sees the Fed’s mission very differently. He views the Fed solely as a defender of what he categorizes as “America’s interests” by backing the administration’s policy decisions.
Against this backdrop, it’s not terribly surprising that market participants have gotten some very mixed messages — both from and about the Fed. So while the Fed’s annual gathering at Jackson Hole always garners a great deal of attention in an otherwise sleepy time in markets, the stakes have been raised by the varied objectives that different stakeholders appear to be pursing. So Powell’s most pressing job is going to be both in getting key Fed officials all on the same page, and then effectively and consistently communicating that message to an increasingly conflicted and nervous constituency.

Nothing about this appears very easy...for the Fed chair or for market participants.

See the UBS House View Weekly, 26 August, 2019.