First Trust
Monday Morning OUTLOOK
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Previewing the Fed

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The Federal Reserve meets on Wednesday and there's one thing we know for sure: it's going to raise rates by another 25 basis points, lifting the federal funds rate to a range from 2.00 to 2.25%.

Why are we so confident? Two reasons. First, the market in federal funds futures is putting the odds of a September rate hike at 99%. For the Fed to let those odds get so high without pushing back forcefully with speeches and leaks to friendly reporters means the Fed is fully on board.

Second, and much more important, it's the right thing to do. Nominal GDP – real GDP growth plus inflation – is up 5.4% in the past year and up at a 4.6% annual rate in the past two years. An economy growing at that pace calls for higher short-term rates.

But the meeting is not only about changing the level of short-term rates; it's also about signaling the path of future rate hikes as well as the continued reduction in the size of the Fed's balance sheet, which became bloated during and after the financial crisis a decade ago.

Back in June, the last time the Fed issued economic projections, it forecast that real GDP would be up 2.8% this year and 2.4% next year. But, given the momentum in the economy, we think the Fed may lift these forecasts. It may also want to reconsider its projections for inflation now that its favorite measure of inflation – the PCE deflator – is already up 2.3% from a year ago

In turn, that should translate into a more aggressive "dot plot," as well. In June, the consensus at the Fed – the "median dot" – showed a total of four rate hikes this year, with one more hike in September and a last one in December. But *almost* half of the voters at the Fed had the Fed stopping at the third rate hike this year or maybe even stopping at two in June. That's going to change substantially on Wednesday and we expect a large majority at the Fed projecting a fourth rate hike in December.

Our best guess is that the median dot will still show three rate hikes in 2019, but that may change in December, by which time the Commerce Department will have reported strong real GDP growth for the third quarter.

In the end, we expect four more rate hikes in 2019. That would take the federal funds rate to a range of 3.25 to 3.5%. Right now, that's not what the market expects. The market is putting the odds of four rate hikes or more next year at 5%. As the economy continues to impress, look for those odds to soar over the next several months. In turn, that means long-term Treasury yields keep trending higher, as well.

The Fed may also consider using Wednesday's meeting to change some wording that's been in every Fed statement since December 2015, which was the first time the Fed raised rates after the financial crisis. The language is "The stance of monetary policy remains accommodative, thereby supporting strong labor market conditions and a sustained return to 2 percent inflation."

Some at the Fed may think Wednesday's rate hike means monetary policy is no longer accommodative. That would be a mistake. But others may want to rightly change the wording because inflation already exceeds 2%. As a result, the Fed needs to start considering how tight it may eventually have to get to keep inflation from staying above 2%.

Just remember, though, that nothing the Fed does on Wednesday is worthy of obsession. Just because the financial media dwells on every word from the Fed, doesn't mean investors should. Instead, focus on profits, which, continue to point to a robust bull market.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
9-26 / 9:00 am	New Home Sales – Aug	0.630 Mil	**0.624 Mil**		0.627 Mil
9-27 / 7:30 am	Initial Claims – Sep 22	210K	**220K**		201K
7:30 am	Q2 GDP Final Report	4.2%	**4.1%**		4.2%
7:30 am	Q2 GDP Chain Price Index	3.0%	**3.0%**		3.0%
7:30 am	Durable Goods – Aug	+1.9%	**+2.1%**		-1.7%
7:30 am	Durable Goods (Ex-Trans) – Aug	+0.4%	**+0.6%**		+0.1%
9-28 / 7:30 am	Personal Income – Aug	+0.4%	**+0.4%**		+0.3%
7:30 am	Personal Spending – Aug	+0.3%	**+0.3%**		+0.4%
8:45 am	Chicago PMI	62.0	**64.5**		63.6
9:00 am	U. Mich Consumer Sentiment- Sep	100.5	**100.8**		100.8