First Trust
Monday Morning OUTLOOK

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Don't Obsess About the Fed

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When it comes to monetary policy, one thing looks certain for 2019 - journalists, pundits, investors, and analysts will pay it way more attention than it deserves. The spotlight is currently on Wednesday, when the Federal Reserve will issue their first statement of the new year. The consensus expects no changes in rates, and we agree.

What would justify heightened concerns? If investors believe monetary policy is about to get overly tight. But that point is still a long way off. Nominal GDP – real GDP growth plus inflation – is up at a 4.8% annual rate in the past two years, well above the 2.375% target for the federal funds rate or the 2.40% the Fed pays banks to hold reserves.

It's true, the Fed is also reducing its balance sheet, but it is doing so at a gradual pace of up to $50 billion per month. That "up to" part is important because in many months the Fed will not have enough securities maturing to hit that $50 billion figure. On top of that, reports suggest the Fed is rethinking how large to keep its balance sheet, potentially leaving it larger than many anticipated. We think that'd be a mistake, but, if anything, it would represent a looser stance for future monetary policy.

In the short-term, the Fed is likely to keep its language on assessing "realized and expected economic conditions," and Fed Chairman Jerome Powell will probably mention "data dependency" at the press conference following the meeting (the press conferences will now be held after every meeting, up from once per quarter).

Unfortunately, the Fed will not only be guided by economic data, but market fears that the yield curve could invert. We think if the Fed lifted rates as the economy grew, the yield curve would move too, not inverting until the Fed was truly tight. But for fear of "what if?" the Fed will likely keep a "buffer zone" of about 40 basis points between the yield on the 10-year Treasury Note and the federal funds rate.

If that holds true, an easy rule of thumb is that we won't see the Fed raise rates again until the 10-year yield hits 3.00%, we won't see a second hike until we get a yield of 3.25%, and won't see a third hike until the 10-year hits 3.50%.

Instead of obsessing about monetary policy, investors should spend their time this year focused on the resilience of the economy. For example, in spite of the partial government shutdown, initial claims for jobless benefits hit 199,000 in the week ending January 19, the lowest since 1969. And auto analysts are forecasting solid sales of cars and light trucks for the month. In other words, the data shows no justification for doom and gloom.

Nothing lasts forever, economic expansions included. But fueled by entrepreneurship, deregulation, and tax cuts, we expect this expansion - and corporate profits - to climb higher. Let others waste their time dwelling on the Fed, wise investors have more important things to think about.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
1-30 / 7:30 pm	Q4 GDP Advance Report	2.6%	**2.5%**		3.4%
7:30 am	Q4 GDP Chain Price Index	1.7%	**1.6%**		1.8%
1-31 / 7:30 am	Initial Claims – Jan 28	215K	**211K**		199K
7:30 am	Personal Income – Dec	+0.5%	**+0.4%**		+0.2%
7:30 am	Personal Spending – Dec	+0.3%	**+0.2%**		+0.4%
8:45 am	Chicago PMI – Jan	60.8	**63.5**		63.8
2-1 / 7:30 am	Non-Farm Payrolls - Jan	165K	**160K**		312K
7:30 am	Private Payrolls – Jan	185K	**160K**		301K
7:30 am	Manufacturing Payrolls – Jan	19K	**16K**		32K
7:30 am	Unemployment Rate – Jan	3.9%	**4.0%**		3.9%
7:30 am	Average Hourly Earnings – Jan	+0.3%	**+0.2%**		+0.4%
7:30 am	Average Weekly Hours - Jan	34.5	**34.4**		34.5
9:00 am	ISM Index – Jan	54.0	**54.0**		54.3
9:00 am	U. Mich Consumer Sentiment- Jan	90.7	**90.7**		90.7
afternoon	Total Car/Truck Sales – Jan	17.2 Mil	**17.2 Mil**		17.5 Mil
afternoon	Domestic Car/Truck Sales – Jan	13.2 Mil	**13.3 Mil**		13.4 Mil

Consensus forecasts come from Bloomberg. This report was prepared by First Trust Advisors L. P., and reflects the current opinion of the authors. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.