Daily Economic Update

May 3, 2017

Fed holds rates steady; views Q1 slowdown as transitory

Our Take:

Today's policy statement managed a fairly balanced tone considering a number of soft data releases in recent weeks: most significantly a slowdown in Q1 GDP growth, but also weaker-than-expected payroll and inflation readings for March. The Fed explicitly noted that slower Q1 activity is "likely to be transitory" and that growth should return to a moderate pace even as monetary policy stimulus continues to be gradually pared back. It sounds like their take on Q1 growth was similar to ours: a slowdown in consumer spending appears anomalous given solid fundamentals, while other details were a bit more encouraging, including a pickup in business fixed investment. The statement made little mention of March's disappointing payroll figure, simply noting that recent job gains have been solid on average and that the unemployment rate declined. The Committee did, however, make note of softer core inflation in March, though we would add that about half of the dip in core PCE and CPI inflation reflected lower prices for mobile phone services (something policymakers would be expected to look through). Nonetheless, it is fair to say that underlying inflation remains slightly below the Fed's 2% objective.

Aside from tweaks to the economic assessment, there were no notable changes in today's policy statement. The Committee reiterated their expectation that economic conditions will warrant a gradual removal of accommodation but gave no overt signal on the timing of the next hike. Our forecast assumes the next move will be in June; while we are encouraged by indications the Fed will look past the Q1 slowdown, we think the Committee will want to see evidence of a pickup in economic activity before continuing their tightening cycle. Data releases over the next six weeks supporting our call for GDP growth to rebound to 2.9% in Q2 would help firm up expectations for a hike at the June 13-14 meeting.

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