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Fed: the Phillips curve is flat

■ Fed chairman Jerome Powell made important comments during his press conference ■ Fiscal policy is on an unsustainable path and lasting widespread tariffs would be bad for the US and the world ■ Monetary policy remains accommodative and data-dependent ■ Markets liked the dovish bias in the message

Is it time well spent to watch press conferences of central bank presidents live? I was wondering as I was following on Youtube Jerome Powell's Q&A session with journalists last Wednesday evening. The questions were clear but the answers were often vague. It was reminiscent of the press conferences of Mario Draghi: *"we didn't discuss it"* has become a Frequently Used Answer to a FAQ. Can we expect anything different? After all, market participants (and journalists) hope for clear answers which take away uncertainty fully knowing that central banks can't deliver because they can't precommit. After all the future is fraught with uncertainty.

Yet, the Fed chairman's press conference turned out to be quite interesting after all and it was not only because of the comment that the US is on an unsustainable fiscal path which needs to be addressed the sooner the better or because of his point that lasting widespread tariffs would be bad for American workers. It was also because of the chairman's observations on the drivers of monetary policy. Firstly, there was the clarification that policy was still accomodative although the word had disappeared from the press release. Bond markets liked it and yields went down as the chairman spoke (chart 1). Secondly there was repeated (implicit) insistence on the data-dependency of the Fed's policy, something which echoes Powell's speech at Jackson Hole in August. Thirdly, the FOMC pays attention to financial markets: "*I think either a significant – significant – correction and lasting correction in financial markets or a slowing down in the economy that's inconsistent with our forecast, those are the kinds of things we'd react to*" and "*You know, what we're going to be doing, assuming we stay on this path, is we're going to be carefully monitoring incoming data from the financial markets and from the economy and asking ourselves whether our policy is achieving the goals we want to achieve*".

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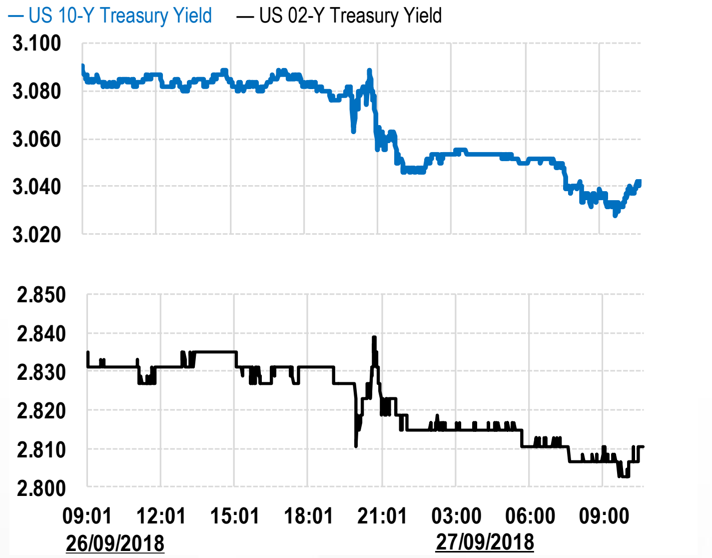
INTRADAY EVOLUTION OF US TREASURY YIELDS*



*The press conference started at 20.30 Paris time and lasted one hour.
Source: Bloomberg, BNP Paribas.

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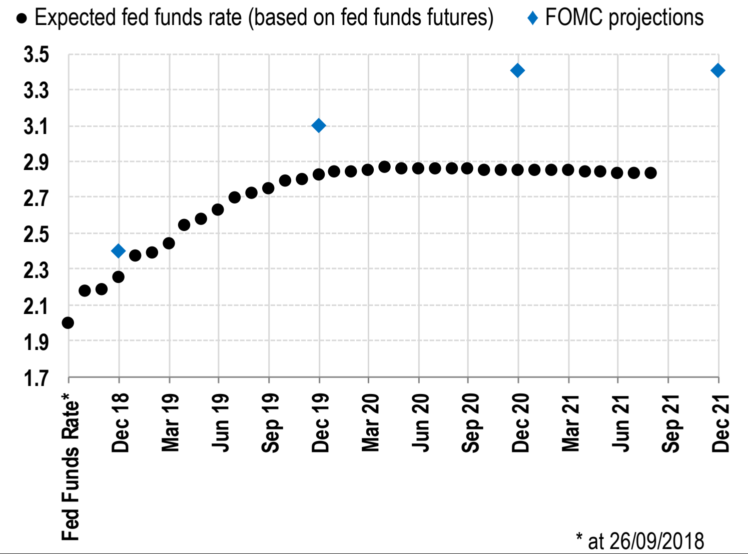
Although to avoid offering a 'Powell put' to the stock market he did add "*But, you know, I wouldn't want to – I wouldn't want to speculate about what the consequences of a market correction should be*". Finally, the significance of the longer term projections was downplayed: "*You know, it's far out into the future. I think it's hard to be confident that that's – that that's the way things are going to be*." All this helps to understand why the expected federal funds rate (which is inferred from futures contracts) is well below the FOMC projections (chart 2). It's not that investors are hearing what the chairman says but are not listening. Quite the contrary: they listen very carefully and, like the FOMC, bet that the Phillips curve will stay flat.

William De Vijlder

EXPECTED FED FUNDS RATE VERSUS FOMC PROJECTIONS



Source: Federal Reserve Bank of St. Louis, CBOT, BNP Paribas