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A Message from Matt Graham:

"I took a few liberties with this one..."

The Day Ahead: What is The Fed Even Thinking?

Today's 'Day Ahead' title is both a rhetorical and literal question. On a literal level, we'll know soon enough, as 2pm brings the latest official policy statement in which the Fed may or may not offer some sort of clue about how a potential December rate hike is shaping up.

On a more incredulous, rhetorical level, what in the world is the Fed thinking? Why would any Fed speaker in their right mind even be talking about a rate hike being a remotely appropriate thing in a world where inflation continues to drop and where domestic economic data has **obviously** begun the 'battleship-in-a-river' turn from the post-crisis expansion.

Don't even get me started on the Fed's newfound consideration of global growth as a domestic inflation risk. Obviously if China is engaging in surprise rate cuts and the ECB is erring on the most dovish side of its equation, the implications are **utterly deflationary** for anything with a $ in front of it.

At times, it sorta seems like a few of them are picking up on these **very basic** policy-related clues. At other times, it seems that they're making up the rules as they go along based on what FEELS right and wrong in terms of where rates should be. "We gotta raise rates because they're too low right now."

Think about that logic. Seriously **think about it.** If rates are too low, and/or if rates are currently in line with a monetary emergency that no longer exists, we have to ask ourselves why we haven't seen ongoing changes in the things that rates are supposed to change. In other words, if rates are "too low," then why isn't inflation increasing and why is economic data sliding in general?

The Fed's retort is that "oil prices are temporarily holding inflation down, but that's just temporary. Once oil prices get back to normal, look out! We could be behind the inflation curve."

Give me a break... I'm not even sure we can rule out that oil price weakness is more to do with **DEMAND** vs supply. Oil prices could be just another symptom of the slowdown that's increasingly playing out in domestic and global economic data. It's naive to assume oil will come charging back, or that it would come charging back so quickly that the Fed would be behind the

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curve in responding to some scary uptick in inflation. I'm **not even sure the Fed believes this stuff** when they say it.

BUT... The Fed isn't dumb.

They keep banging this rhetorical drum for a reason. They're just **not telling us** what the real reason is. Look, I know that sounds rather like an unfounded conspiracy theory, but you'll have to agree that the justification for their level of rate hike admonitions just isn't there. So we have to account for it some other way.

So far, Fed speakers have offered precious few clues about what **really** has them spooked. These have included things like financial stability, bank deposits, and if you really stretch, wealth inequality. I see today's Announcement as a **good opportunity** for the Fed to send a message that they are--in fact--participating in reality. They could do this by acknowledging the recent deterioration in data and could furthermore make no menacing gestures toward a near term hike. OR they could continue the charade (by adding some verbiage that alludes to the possibility of a December hike), thereby sending us right back out into the field to look for more clues as to their **ACTUAL** justification. Hopefully they'll tell us some day.

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