



A statement from Rick Rieder, BlackRock's Chief Investment Officer of Global Fixed Income and Head of the BlackRock Global Allocation Investment Team, regarding yesterday's Fed Policy Statement

Highlights

- The Fed's actions, language and overall tone today were very much like those of a flight crew that has taken on precautionary fuel to make sure the plane can arrive at a yet-to-be-determined destination without problems.
- The fact is that there is great uncertainty regarding the progression of the coronavirus pandemic and the timing of a return to economic normalcy and the Fed has been diligently preparing for this.
- More important than the public statements today were the discussions that took place around the Fed's boardroom table regarding the evolving policy toolkit and potential implementation if things became worse for the economy. However, we may not learn about that until the meeting minutes are released three weeks from now.
- Finally, the key to near-term monetary policy will be all about the Fed's dual mandate, but with one side of the mandate being the primary target (employment) and the other governing how far the central bank is willing to go (inflation).
- The fact is that the Fed likely has an impressively long runway yet, as it could be a very long time before we regain full employment, which didn't even appear to be inflation-accelerating at a 3.5% unemployment rate.

Filling the Plane with Precautionary Fuel

We heard today from the Federal Reserve in a couple of different formats: in both the Fed Statement and in Chair Powell's press conference policymakers displayed a tangible willingness to keep monetary policy historically easy, with a proclivity toward doing more to support the recovery and 'not even thinking about' doing less. As Chair Powell described, the fact remains that there continues to be great uncertainty regarding the progression of the coronavirus pandemic and the timing of a return to economic normalcy. Further, we expect it could be a very long time before we regain full employment (which didn't even appear to be inflation-accelerating at a 3.5% unemployment rate), and clearly this has influenced the Fed to err on the side of more rescue-assistance versus less, and possibly even more going forward than the tremendously aggressive, creative and bold initiatives heretofore undertaken.

Indeed, yesterday's announcement that the central bank would be extending existing programs to the end of the year, alongside of today's statement and the Chair's answers to press questions, is clearly reflective of the Committee's deep commitment to recovering the hard won gains in jobs and growth, which the pandemic has since stripped away. It is almost as if the Fed has decided to fill the economic plane with as much jet fuel as possible, for a flight that at this point has an uncertain destination. In this analogy, having to spend some money on excess fuel for a flight that may be shorter than expected is a sensible cost to bear, when not having enough fuel could create potential problems down the road in terms of time and effort expended to get to the desired destination.

What may have been more important than the public statements today were the discussions that took place around the Fed's impressive boardroom table. Presumably part of this discussion involved the Fed's evolving policy toolkit and potential implementation if things became worse for the economy and employment. However, we may not learn about that until the meeting minutes are released three weeks from now. Potentially, the Fed may also be more explicit on next steps at the September meeting, or conceivably not until the end of the year meeting. But sufficed it to say, the discussion was about how to load more fuel on that plane and not less. Tools such as longer forward guidance, explicit yield curve control, and/or more asset purchases and lending in different forms and sizes are likely all being discussed, even if some of them likely won't ultimately be utilized.

The key to near-term monetary policy will be all about the Fed's dual mandate, but with one mandate being the target (employment) and one being the governor on how far the central bank is willing to go (inflation). We do not believe that the Fed will establish a specific target on employment for policy lift-off, but it will attempt to test where full employment truly is in the economy, which will not come for an extended period. In fact, Chair Powell stressed that the Committee's goal was trying to get the labor market back to a pre-Covid-like state and getting inflation to 2%. Inflation, however, is the Fed's governor on how far the Committee is willing to go, and that too should take a long time before it feels constrained. We think that the Fed is on the road to determining an inflation target of some form of average over time, meaning this Fed will have to overshoot the 2% inflation target for an extended period.

With inflation (as typified by Core PCE) running at 1.0%, as of May, and anticipated to run at 1.0% on average over the next year or so, that governor on additional policy from the Fed will be a long-time in coming. Hence, we think the Fed will keep loading the plane with fuel on the way to our very uncertain destination; essentially until that intended destination is very clearly apparent from the cockpit window. The upside vs. downside risks of policy action, or inaction, was very clear before today's meeting and nothing but reinforcement of that philosophy was apparent in today's actions.