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# TD Economics

**Data Release: FOMC minutes give the go ahead to June hike**

- The minutes from the Federal Open Market Committee's meeting in May showed continued confidence in the labor market recovery among participants and suggested the Committee is comfortable to continue on its path of gradual increases in the federal funds rate.
- Of note, "most participants judged that if economic information came in about in line with their expectations, it would soon be appropriate for the Committee to take another step in removing some policy accommodation."
- The apparent weakness in economic growth and consumer spending early in the year was noted, but the general sense was that it would prove temporary. Weakness in consumer spending was contrasted with the improvement in both residential and non-residential investment – which were deemed as an encouraging sign.
- The Committee's risk assessment remained balanced, with little change in longer-term outlook. However, participants noted financial stability concerns regarding valuations in CRE and that "reforms in the housing finance sector could have implications for such valuations."
- The debate around the two sides of the Federal Reserve's mandate continued, with doves emphasizing inflation's current low readings and expressing concern over expectations, while more hawkish members noted the undershooting of the unemployment rate and the potential for this to lead to an eventual overshooting of inflation.
- The minutes provided some additional detail on reinvestment policy, suggesting that it will soon formally outline its policy and potentially begin shrinking its balance sheet later this year. The outlined approach would set dollar limits on the amount of securities that would be allowed to run off. The pace of runoff would be small initially, but rise over time. Limits would be raised every three months until fully phased-in, at which point they would be maintained until the Fed's balance sheet was normalized.

**Key Implications**

- As long as the labor market continues to generate above-trend job growth (minutes noted 180k monthly in the first quarter), the Fed's bias will be to gradually raise the federal funds rate.
- The one thing that may slow their hand is a continued deceleration in inflation. Ongoing weakness in price growth would support those on the FOMC who see the unemployment rate as either under-reporting the level of economic slack or as not having the explanatory power in predicting inflation that it once did. The Fed, while not giving up on the Phillip's curve, is at least willing to take a wait and see approach.
- The other potential fly in the ointment for ongoing normalization in short-term rates is the desire to also begin normalizing the balance sheet. The Fed's hope is that if telegraphed clearly and far enough in advance, and if done in a gradual and predictable manner, balance sheet normalization will have minimal deleterious effect on financial conditions and can work in tandem with short-term rate increases in gradually removing monetary accommodation.

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