Fed: Markets Need a Lot More Patience With Inflation

A Federal Reserve official says that ‘everybody should just take a deep breath.’

By Erik Sherman

Last Thursday, when the consumer price index numbers for October came out, the markets gave a big thumbs-up. Look at the graphs of the Dow Jones Industrial Average, the S&P 500, Nasdaq, and even the Russell 2000. They all jumped up from 2.7% to 5.7%. It was obvious that the improved inflation numbers were the sort of news the Federal Reserve had wanted.

And, sure, that is true, except, as Fed governor Christopher Waller said in Australia during a UBS hosted function, according to the Wall Street Journal, “The market seems to have gotten way out in front on this. Everybody should just take a deep breath—calm down. We have a ways to go yet.”

Ah, a downer, and stock markets have tempered a bit. This is a reminder to other financial markets, including the commercial real estate industry, that value and advantage tend to grow over time, not the sudden presentation of a benefit like a lottery ticket.

“While the Fed is encouraged by the tame reading in the latest CPI report, it will require more than one month for evidence that it’s time to throttle back its rate-hiking campaign,” Oxford Economics wrote. “Fed officials are more concerned about prematurely easing its foot off the brake than overshooting the rate increases needed to curb inflation. In their defense, we have seen false dawns in this inflation cycle before, most notably in the summer of 2021 when, after a brief slowdown, price gains reaccelerated with a vengeance. That said, there is compelling evidence that the inflation peak is behind us, and the retreat should continue.”

And according to a Capital Wealth Planning note, “The CPI report was a step in the right direction, but from the Fed’s standpoint, nothing has changed and it will continue to push the terminal rate toward 5%.” Currently, the federal funds rate—the Fed’s benchmark—tops out at 4%. If Capital Wealth’s view is correct, that could mean another two 50-basis point increases left to go, assuming that would finally get the result the Fed has wanted.

Maybe, as that firm suggests, “inflation has potentially peaked.” But if that ultimately slows inflation to the desired 2% level, what happens then? Remember, at that point the resulting financing rates are that much higher than today, and, realistically, closer to historical norms than the roughly 15 years since the global financial crisis. There’s an extremely good chance that what the industry sees today is the long-term future, not a short aberration. Everyone may be holding that deep breath, as Waller said, for a long time.