Weekly Commentary

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Aggressive Fed

Behind the scenes of December's Federal Reserve policy meeting, participants broached the third step of the process to remove accommodation. In the statement following the Federal Open Market Committee meeting last month, they publicly announced an acceleration of the pace at which the Fed is reducing its monthly purchases of U.S. Treasuries and agency mortgage-backed securities and projected more rate hikes than previously thought. But revealed in the minutes to that meeting released last week, in private, the topic of the Fed's massive balance sheet of these securities arose. "Almost all participants agreed that it would likely be appropriate to initiate balance sheet runoff at some point after the first increase in the target range for the federal funds rate."

This development seems to show just how serious policymakers are about their pivot in the latter part of 2021. If they start the wind-down process in the heart of a rising rate cycle, they would deviate from the last low-rate period of approximately 2012-19. The reason for the current accommodation of course is leagues removed from that one, so the comparison yields less information. Aggressive Fed action has the potential to benefit the liquidity markets, but there are still many unknowns.

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