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Weekly Commentary

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Paige Wilhelm
Senior Vice President
Senior Portfolio Manager
Federated Investment Counseling

Powell might have to start shouting

Now you see why Jerome Powell spoke in such direct terms in Jackson Hole, Wyo. The Federal Reserve chair reiterated policymakers' resolve to restore price stability, with the subtext being they need the labor market to cool to achieve that. But it has not been following the script.

The latest indication came with the August employment report released last Friday that showed employers added 315,000 jobs. On the heels of July's massive increase of 526,000, it would seem the Fed will have to continue to tighten policy to get businesses to slow hiring. The idea is that if company management thinks the economy is slowing and consumers are losing their appetite to spend, they will curtail production and activity. That should limit the number of new workers they bring aboard and lessen the need to pay higher wages.

That storyline clearly is not unfolding in this economy still warped by the pandemic. The unemployment rate rose in August to 3.7%, the first time it has climbed since January. Typically, this could mean companies are shedding workers as they expect economic contraction. But this time it is more likely that people who had stopped looking for a job have started searching again—which means they are now counted among the unemployed. Evidence for this comes with the bump in the labor participation rate.

If higher inflation is forcing people to regain an income stream, it might mean the rate hikes are having an effect without damaging the economy. The Fed would like this scenario as it suggests inflation might recede without a recession. But it probably needs to remain aggressive, increasing the likelihood it will hike rates by 75 basis-points in the upcoming FOMC meeting.

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