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Gregory Cater Sr. and Gregory Cater Jr.
 The Fed Has Gone Too Far

On September 21st 2022, the Federal Reserve raised its benchmark interest rate 75 basis points for the 3rd time in a row. The rate 6 months ago was .25%, today its 3.25%. In his press conference Fed Chair Powell suggested another 100 to 125 basis point increases in the next two meetings. The first paragraph of his statement reads:

“Recent indicators point to modest growth in spending and production. Job gains have been robust in recent months, and the unemployment rate has remained low. Inflation remains elevated, reflecting supply and demand imbalances related to the pandemic, higher food and energy prices, and broader price pressures.”

He goes on to say:

“The Committee is strongly committed to returning inflation to its 2 percent objective”

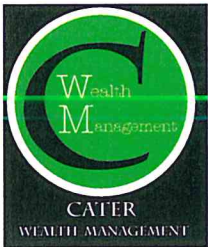
I will grant inflation is too high and needs to be brought down. Before we panic, let’s take a deep breath and look at the recent releases.

	CPI	CPI(CORE)	CPI(YOY)	PPI	Import Prices	Export Prices
June’22	1.1%	0.7%	9.1%	2.7%	0.2%	1.0%
July’22	0.0%	0.3%	8.5%	(-1.8%)	(-1.5%)	(-3.7%)
Aug’22	0.1%	0.6%	8.3%	(-1.2%)	(-1.0%)	(-1.6%)

The Consumer Price Index (both headline and core), as well as the Producer Price Index and both Import Prices and Export Prices seem to have peaked in June. After peaking at 1.1% in June CPI is basically unchanged through Aug. CPI(YOY) has declined and PPI, Import Prices and Export Prices are falling (deflation?). When the Fed says its goal is to bring inflation back to its 2% objective it isn’t saying it wants to bring prices back to where they were last year, it is saying it wants prices to stop going up so much. Deflation is not its goal. Here’s the problem. Everyone focuses on year over year inflation. In the last year inflation was up 8.3%. It peaked at 9.1% in June and has fallen to 8.3% but it’s still too high. We should be focusing on where inflation is now, not where it was last year. We can only influence now, we can’t change history. If we don’t want deflation (and we don’t, trust me) we are making progress on bringing inflation back down to 2%.

The Fed sees: “Inflation remains elevated, reflecting supply and demand imbalances related to the pandemic, higher food and energy prices, and broader price pressures.”

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I see: Price declines from peak earlier this year

Copper	down	30%
Wheat	down	31%
Lumber	down	58%
Soybeans	down	19%
Corn	down	17%
Oil	down	35%

Measuring CPI YOY is simple math. We start with Aug'21 CPI (273.092) and end with Aug'22 CPI (295.62). We get 8.30%.

The last 2 months CPI has been flat. The next 4 months of this year will be compared to the last 4 months of last year.

Sept'21	274.21
Oct'21	276.59
Nov'21	278.52
Dec'21	280.13

If the inflation rate reported in the next 4 months (Sept through Dec) is 0.0%, the CPI(YOY) will fall to 5.50%. If the inflation rate reported in the next 4 months matches exactly the Feds 2% target, CPI(YOY) will be 6.2%.

The Fed has been increasing rates for 6 months. We have experienced 2 months of lower inflation and even if we continue seeing success in keeping price increases to the 2% target the Fed will still see inflation running at 3 times its objective.

I think history will judge the last 75 basis points a mistake. The world is most likely in a recession. In the US the 1stQ GDP was (-1.6%), 2ndQ GDP was (-0.6%) and the Atlanta GDPNOW model is projecting 0.3% for the 3rdQ. The Fed is looking for full year 2022 GDP at an anemic 0.2%.

The Fed is raising rates and tightening financial conditions on the cusp of a worldwide recession and falling prices.

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