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PHILEQUITY CORNER

By Wilson Sy

Higher for longer

Last Friday, Federal Reserve (Fed) Chair Jerome Powell made his much-awaited keynote speech at the Jackson Hole economic symposium. He warned that inflation is still too high while signaling that the Fed is ready to raise rates further if needed. Powell’s comments propelled the US dollar index (DXY) above 104. Bond yields remained high while equity markets continued to be volatile.

Woodstock for economists

The annual symposium in Jackson Hole is considered the holy grail for economists and central bankers. It is an event where central bankers share their policy outlook and discuss their rationale behind it. During the symposium, policymakers explain major programs that they would pursue. In the past, Fed chiefs made important speeches in Jackson Hole that drove the direction of the stock market and other asset classes for many years. As such, it is a must for investors to follow policy statements made in Jackson Hole.

We regularly wrote about the Fed’s policy pronouncements in Jackson Hole due to their important implications to financial markets and the economic outlook. In his 2010 Jackson Hole speech, ex-Fed chair Ben Bernanke explained the logic behind the Fed’s massive bond-buying program which is now known as quantitative easing (QE). It was in Jackson Hole where Bernanke displayed his willingness to undertake unconventional policies to revive the economy from the impact of the 2008-2009 global financial crisis. In a complete reversal of policy, Powell was in full hawk mode when he warned that failing to restore price stability would result in a far greater pain (see *Hawk at Jackson Hole*, August 29, 2022).

The Jackson Hole hawk

In his recent speech, Powell clarified that inflation remains too high despite easing from its recent peak. Powell warned that recent readings of above-trend growth may stoke inflation and necessitate further tightening. Below, we list important quotes from Powell’s latest Jackson Hole statement.

- “Although inflation has moved down from its peak—a welcome development—it remains too high.”

- “We are prepared to raise rates further if appropriate, and intend to hold policy at a restrictive level until we are confident that inflation is moving sustainably down toward our objective.”

- “The lower monthly readings for core inflation in June and July were welcome, but two months of good data are only the beginning of what it will take to build confidence that inflation is moving down sustainably toward our goal.”

- “But we are attentive to signs that the economy may not be cooling as expected. So far this year, GDP growth has come in above expectations and above its longer-run trend, and recent readings on consumer spending have been especially robust.”

- “Additional evidence of persistently above-trend growth could put further progress on inflation at risk and could warrant further tightening of monetary policy.”

- "We cannot identify with certainty the neutral rate of interest, and thus there is always uncertainty about the precise level of monetary policy restraint."

- "Doing too little could allow above-target inflation to become entrenched and ultimately require monetary policy to wring more persistent inflation from the economy at a high cost to employment. Doing too much could also do unnecessary harm to the economy."

Hawkish pause

Last month, we wrote about the hawkish pronouncements of newly-appointed Bangko Sentral ng Pilipinas (BSP) Governor Eli Remolona (see *Structurally hawkish*, July 24, 2023). In recent interviews, he explained that the BSP is in a hawkish pause because inflation is still not comfortably within the target range. Below, we summarize Remolona's important comments on monetary policy, inflation, and the peso.

- "We're in a hawkish stance, which means either we pause or we raise for the time being." "I think we have room to hike without contracting the economy,"

- "A hawkish pause is the right way to describe it. We go where the data leads us. But the data seems to be going in two different directions, so I think a pause is prudent."

- "We're ready to hike if the upside risks materialize."

- "It's a balancing act. We try to figure out how strong the lag effects are and how expectations are evolving."

- "What is more effective than intervention is forward guidance. So, we give the market a better idea of what we are thinking about down the road. That seems to be more effective, that seems to have stabilized the peso."

- "There is some volatility, more than usual, but we see it as an issue of being a strong dollar than a weak peso. The currencies of our neighbors, the Thai baht and the Malaysian ringgit, have weakened along with the peso in the last few days."

Hawkish stance

As we have seen in the past, the Jackson Hole speeches of central bankers carry added significance because they outline major policy programs that could last for many years. It is therefore essential for investors to take their cues from Powell's latest Jackson Hole statement. The recent hawkish comments made by Powell and Remolona highlight the need for central bankers to remain vigilant in bringing down inflation and extinguishing any chances of its resurgence. The hawkish stance of central bankers coupled with the recent credit rating downgrades (see *Fitch downgrade hurts markets*, August 7, 2023; *Moody's downgrades US banks*, August 14, 2023) results in a scenario where interest rates would remain higher for longer. In fact, this has spurred the surge of the US dollar, the big drops in equity markets, and the fall of bond prices. Higher interest rates would indeed tame inflation eventually but these would also hamper economic growth, increase recession risk, and usher financial market volatility.

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