

## The Fed Reacts to Higher-Than-Expected Inflation

Two weeks ago, there was broad acceptance by the market that the Federal Reserve would increase its overnight rate by 0.50% at its June 14-15 Federal Open Market Committee (FOMC) meeting. Those perceptions began to shift after the Labor Department reported on Friday, June 10<sup>th</sup> that May's consumer price index (CPI) increased from May 2021 by 8.6%, which marked a new 40-year high. The increases in what consumers pay for goods and services was broad based, but the main driver was increases in energy prices. The energy index component of the CPI increased 34.6% over the same 12-month period. That same day it was reported that the average price of gasoline in the U.S. hit a new nominal high of \$5.00 per gallon.

Another measure of changes in price levels is the producer-price index (PPI), which measures what suppliers are charging businesses and other customers. On Tuesday, June 14<sup>th</sup> the May PPI was released and it was up 10.8% over the previous 12 months, which marked the sixth straight month of double-digit gains for the index.

With fresh inflation data the Federal Reserve departed from its recent guidance and announced on June 15<sup>th</sup> that it would increase its overnight rate by 0.75%, bringing the range to 1.50%-1.75%. Additionally, and perhaps more importantly, median projections by the FOMC meeting participants now have the fed-funds rate increasing an additional 1.75% during 2022 and rising to 3.75% by the end of 2023. At the June 15<sup>th</sup> news conference Fed Chairman Jerome Powell noted that based on current economic conditions either a 0.50% or 0.75% increase would be likely at the July FOMC meeting.

### FOMC Meeting Statements

Date	Federal Funds Rate		Balance Sheet (Monthly)	
	Increase	Target Range	Reduction	Target
prior		0.00% - 0.25%		\$120 billion
Nov 3, 2021	--	0.00% - 0.25%	(\$15 billion)	\$105 billion
Dec 15, 2021	--	0.00% - 0.25%	(\$45 billion)	\$60 billion
Jan 26, 2022	--	0.00% - 0.25%	(\$40 billion)	\$20 billion
Mar 16, 2022	0.25%	0.25% - 0.50%	(\$20 billion)	--
May 4, 2022	0.50%	0.75% - 1.00%	(\$48 billion)	(\$48 billion)
Jun 15, 2022	0.75%	1.50% - 1.75%	--	(\$48 billion)
Jul 27, 2022*	0.50%	2.00% - 2.25%	--	(\$48 billion)

\* Lower range of increase based on June 15, 2022 comments by Chair Powell

It has been a rough go for most broad-based measurers of stocks and bonds since the Fed announced that it would begin tightening on November 3<sup>rd</sup>, 2021. Higher rates have caused bond prices

to fall with longer duration indices down over 10%. The S&P 500 moved into bear territory on Monday of this week as the index was down 20% from its previous high. That stated, the capital markets seemed receptive to the Fed's actions on June 14<sup>th</sup> with markets rallying that afternoon, but the rally was short-lived, as Thursday's markets moved lower with the Dow Jones Industrial Average ending the day below the 30,000 level for the first time since January 2021.

A notable milestone occurred this week with the average rate on a 30-year, fixed rate mortgage in the U.S. exceeding 6.00%, according to Mortgage News Daily. Increased mortgage rates have helped to cause home sales to decline for six straight months.

### Municipal Market Update

Interest rates on municipal bonds continue to move higher across the yield curve as illustrated by the following chart which provides Municipal Market Data (MMD) AAA yields since the start of 2020 for 5-year, 10-year, and 20-year maturities.



In response to rising rates, investors continue to sell municipal bonds as evidenced by the fact that net municipal bond outflows have occurred in 20 of the past 21 weeks.

PMA is dedicated to staying up to date on market trends and will be ready to guide you through a dynamic and evolving market. If you have any questions about the municipal bond market in general or your specific bond issue, please feel free to contact a PMA advisor below.



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