NEWSQUAWK PREVIEW: Federal Reserve rate decision due Wednesday 21st September 2022 at 19:00 BST/14:00EDT; Chair Powell press conference at 19:30BST/14:30EDT

- **Expected to hike 75bps to 3.00-3.25%, while markets are pricing a 20% chance of 100bps.**
- **Spike in August CPI removes opportunity for any near-term relent on tightening plans.**
- **Dot Plot to show higher terminal rate forecast with market pricing at 4.5% and sell side estimates ranging up to 5%.**

75 OR 100: The FOMC is expected Wednesday to hike the FFR by 75bps to 3.00-3.25%, with risks of a larger 100bps hike after the super-hot August CPI data shattered expectations for any imminent downturn in inflation. While the angst around CPI is deafening, it's worth highlighting the decline in long-term inflation expectations (via UoM and NY Fed surveys), lower prices paid components in September Philly Fed and Empire State releases, and also the more contained August PPI data (which will keep the Fed's preferred inflation gauge, Core PCE, more anchored) as factors that may temper some of the extreme hawkishness, ergo votes for 100bps.

MARKET PRICING: Markets took down implied 100bps September pricing to near 15% in wake of the decline in the UoM consumer inflation expectations survey, although crept back up to 20% as of Monday. Money markets have priced in just shy of 150bps of hikes across the September and November meetings, with 190bps priced through December, taking the 2022-end rate into a 4.00-4.25% range up from 3.75-4% before CPI, while 215bps of tightening is currently priced into the terminal rate (March 2023) taking rates towards the top-end of the 4.25-4.5% range up from 3.75-4% pre-CPI. Markets are currently pricing a 2023-end Fed rate at 4%.

GUIDANCE: The broad-based upside seen in the August CPI (Core +0.6% M/M, +6.3% Y/Y, with services gaining momentum) broke what could have been more evidence toward a series of lower readings, a condition that would have allowed the Fed to start considering a slowdown in the pace of tightening. With the dovish runoff now closed, at least in the near term, the likelihood of the Fed hiking until the economy crashes, a 'hard landing', has increased further and markets have shifted to reflect that notion. Aside from risks of 100bps in September, another 75bps in November looks more likely. Fed officials have stressed their data-dependence and have on the whole been coy to tie their hands to guidance on the rate path. We can expect a reiteration in the statement, "the Committee... anticipates that ongoing increases in the target range will be appropriate." Powell will likely be pressed on his preference for the November meeting in the press conference. Absent guidance, the data-dependent stance will instead see greater attention put on the SEPs.

DOT PLOT: The SEP ('Dot Plot') will be updated, since their last iteration in June, to show both a higher year-end and terminal rate with some desks in wake of CPI forecasting new dots that could reach heights of 4% (prev. 3.4% median in June) and 5% (prev. 3.8% in June), respectively, reflective of both the worsening inflation outlook and stubbornly tight labour market. Fed Governor Waller, to wit, "right now there is no tradeoff between the Fed's employment and inflation objectives, so we will continue to aggressively fight inflation." However, there is no clear consensus among analysts for the terminal rate, but forecasts are seen more common around 4.25%, with some dovish estimates pencilling in a terminal beneath 4%. A few are also forecasting rate cuts heading into 2024 and 2025.

Bloomberg compiled the following economist survey between September 9th-14th, meaning not all responses will incorporate the August CPI data, thus, these can be considered somewhat stale, with expectations for the Fed Funds and inflation dots having nudged higher since the data. Note this is also the first SEP release containing 2025 estimates.

Median dot expectations:

- FEDERAL FUNDS RATE: exp. at 3.9% in 2022 (prev. 3.4% in Jun), 4.1% in 2023 (prev. 3.8%), 3.6% in 2024 (prev. 3.4%), 2.9% in 2025, 2.5% in longer run (prev. 2.5%)
- CHANGE IN REAL GDP: exp. at 0.5% in 2022 (prev. 1.7% in Jun), 1.4% in 2023 (prev. 1.7%), 1.7% in 2024 (prev. 1.9%), 1.8% in 2025, 1.8% in longer run (prev. 1.8%)
- UNEMPLOYMENT RATE: exp. at 3.7% in 2022 (prev. 3.7% in Jun), 4.1% in 2023 (prev. 3.9%), 4.2% in 2024 (prev. 4.1%), 4.1% in 2025, 4% in longer run (prev. 4.0%)

- PCE INFLATION: exp. at 5.2% in 2022 (prev. 5.2% in Jun), 2.6% in 2023 (prev. 2.6%), 2.2% in 2024 (prev. 2.2%), 2% in 2025, 2% in longer run (prev. 2.0%)
- CORE PCE INFLATION: exp. at 4.5% in 2022 (prev. 4.3% in Jun), 2.8% in 2023 (prev. 2.7%), 2.3% in 2024 (prev. 2.3%), 2% in 2025

BALANCE SHEET: Fed officials are also likely to be increasingly cognizant of the restrictive effects of quantitative tightening (QT), both from a monetary perspective and a smooth market functioning view, with liquidity conditions in the Treasury market sitting at uncomfortable levels from a historical standpoint. These concerns have brought uncertainty about whether the Fed will go ahead with previous stated plans to consider MBS sales. Note, the runoff (allowing existing holdings to mature without reinvesting) has now accelerated to an annual pace of USD 1.1tln, while desks see the balance sheet shrinking to USD 8.4tln by year-end and USD 6.6tln in December 2024, based on the current plans.