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A history of reactions to the FOMC

If this wasn't an FOMC meeting that had a press conference and fresh economic projections, there would be no point in hitting the World Cup pause button. But a look at market reactions to FOMC meetings over the past two years is clear about one thing – FOMC meetings with press conferences have consistently generated large moves, and much larger price changes than meetings without press conferences.

1. Volatility

Table 1 looks at the absolute median market response on the last day of FOMC meetings when there is and is not a press conference. Table 3 provides more detail.

Table 1: Median of the absolute 1 day change in asset markets on FOMC press conference days when FOMC only issues a statement

	S&P 500 (% change)	2 yr yield (change in bps)	10 yr yield (change in bps)	USD/EUR (% change)	USD/JPY (% change)	USD/AUD (% change)
Press conference	0.94	2	6	0.65	0.91	0.54
No press conference	0.35	1	4	0.20	0.34	0.50

Source: Deutsche Bank, EcoWin, Federal Reserve Board

USD/JPY moves are consistently large on FOMC press conference days when compared with days when the FOMC finishes with only the regular statement. The smallest absolute percentage change in USD/JPY on an FOMC press conference day is 0.42%, which is the second largest absolute change on a FOMC day when only a statement is released! The same pattern is evident in EUR/USD where the median of the absolute percentage change in EUR/USD was 0.65% on press conference days, and a very subdued 0.20% median on days when FOMC ended with no press conference. The above message was largely echoed in equities price action, and slightly less so in Treasuries.

What is evident is that 'more' information initially translates into greater volatility on press conference days. A week later, data shows that a press conference has no lasting impact on the absolute change in any of the above instruments relative to the aftermath of non-press conference FOMC meetings.

2. Directional bias

Table 2 below shows a strong bias for FOMC press conference days to result in higher 10y yields (6 of last 8 meetings) and a very similar story of USD/JPY going up in the same 6 of the last 8 FOMC meetings with press conferences.

Table 2: Median of the 1 day change in asset markets on FOMC press conference days when FOMC only issues a statement

	S&P 500 (% change)	2 yr yield (change in bps)	10 yr yield (change in bps)	USD/EUR (% change)	USD/JPY (% change)	USD/AUD (% change)
Press conference	0.36	1	5	-0.26	0.90	-0.07
No press conference	-0.35	0	-1	-0.01	-0.04	0.41

Source: Deutsche Bank, EcoWin, Federal Reserve Board

The USD in contrast had a downward bias versus the EUR on press conference days and otherwise showed no directional bias on non-press conference FOMC days.

Unlike the clear tendency for the long-end to sell-off on FOMC press conference days, the short-end response has been benign probably because any perceived Fed hawkishness is relevant for fed funds far into the future, and better played through the intermediate and long-end. A mix of the projections and the inclusion of all FOMC participant 'dots' is one reason for the negative back-end reaction. Equities have in the past taken higher bond yields on the chin, and surprisingly done better on press conference days.

Where does this leave the market?

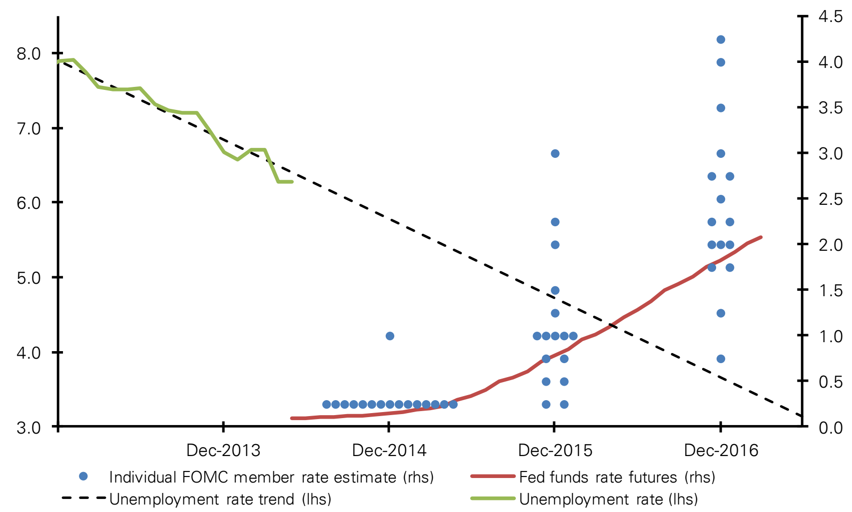
Firstly don't underestimate the mix of new forecasts; new FOMC 'dots' and most important the Q&A, to result in surprises and some volatility.

Janet Yellen probably has no interest in correcting market expectations at this stage, because a rate hike is still seen by a majority of the Fed as many months, if not a year away and expectations are not unreasonably out of line with the Fed's own views. New geopolitical concerns and the risk of higher oil prices are adding to uncertainties and further argue against the Fed directing expectations with any certainty. Yellen is then probably a couple of FOMC meetings away from being under any real pressure to adjust market expectations, assuming recent growth and inflation trends persist.

In the meantime, what is less predictable is what happens if the Fed Chair is asked some difficult questions, notably on the likely gap between tapering and tightening that led to her infamous '6 month' comment. Another market sensitive line of questioning, will be on her views about secular stagnation and the neutral funds rate. Does she believe in a new neutral funds rate? It would not be a huge surprise to find out that Yellen's views on this subject are not too far off the recent Dudley comments that made a case for a slightly lower natural rate of interest. It is also quite possible that the dots on the longer-run funds rate will come down to the point where the median is below 4%. The market will get excited, even if this is merely following the slow drift lower in the Fed's central projections on longer-run real GDP that was 2.2% - 2.3% in March, having come down nearly 0.5% from FOMC estimates 3 years ago.

A more dovish view on the fed fund dots in the longer-run, could partially offset any sign of slightly less dovish dots for end 2015 and end 2016, but presumably the 2 to 5 year sectors would still suffer if 2015 and 2016 dots drift higher, and the USD will gain some important additional support. So far in June, the market has priced in an additional 25bp of rate hikes for Dec 2016, but the market is still some 43bps more dovish than the FOMC median dots, leaving plenty of scope for additional front-end USD support, as the market catches up with a Fed reluctant to provide much in the way of fresh rate signals for now.

Figure 1: Fed fund futures versus FOMC dots



Source: Deutsche Bank, EcoWin, Federal Reserve Board, Bloomberg Finance LP

Table 3: Asset response to FOMC meetings with press conferences (changes during day)

	S&P 500 (% change)	2 yr yield (change in bps)	10 yr yield (change in bps)	USD/EUR (% change)	USD/JPY (% change)	USD/AUD (% change)
6/20/2012	-0.17	2	3	-0.13	0.75	-0.05
9/13/2012	1.63	-1	-3	-0.70	-0.42	-0.72
12/12/2012	0.04	0	5	-0.52	0.90	-0.23
3/20/2013	0.67	1	5	-0.39	0.93	-0.10
6/19/2013	-1.39	4	17	0.74	1.20	2.09
9/18/2013	1.22	-5	-16	-1.22	-1.19	-1.72
12/18/2013	1.66	1	6	0.61	1.56	0.36
3/19/2014	-0.61	8	10	0.74	0.90	0.96
Median	0.36	1	5	-0.26	0.90	-0.07
Average	0.38	1	3	-0.11	0.58	0.07

Source: Deutsche Bank,, EcoWin, Federal Reserve Board

Table 4: Asset response to FOMC meetings when only a regular statement is delivered and there was no press conference (changes during day)

	S&P 500 (% change)	2 yr yield (change in bps)	10 yr yield (change in bps)	USD/EUR (% change)	USD/JPY (% change)	USD/AUD (% change)
8/1/2012	-0.30	2	6	0.65	0.41	0.40
10/24/2012	-0.31	0	2	0.12	-0.05	-0.86
1/30/2013	-0.39	-1	0	-0.55	0.37	0.58
5/1/2013	-0.93	-1	-4	-0.08	-0.03	0.91
7/31/2013	-0.01	0	-2	-0.28	-0.17	0.90
10/30/2013	-0.49	0	3	0.08	0.33	-0.04
1/29/2014	-1.02	1	-7	0.05	-0.65	0.42
4/30/2014	0.30	-2	-5	-0.40	-0.36	-0.16
Median	-0.35	0	-1	-0.01	-0.04	0.41
Average	-0.39	0	-1	-0.05	-0.02	0.27

Source: Deutsche Bank, EcoWin, Federal Reserve Board