Market View
Biding their time: the politicisation of central banks

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At a glance

- Recent events appear to have turned the tides for Biden who was relying on benign inflation for his re-election this year.
- Although growth remains resilient, recent data indicates inflation will remain stickier for longer.
- The Federal Reserve announced that they would slow the pace of its Quantitative Tightening program beginning in June.

At the start of 2024, the pieces appeared to be falling in place for President Joe Biden in his re-election year. His main opponent, Donald Trump, was marred with 88 criminal counts and set to appear in various court proceedings throughout the year.[1] This allowed Biden a rare opportunity to woo his electorate with popular policies such as student loan forgiveness.

Biden was also counting on benign inflation, allowing the Federal Reserve (Fed) to begin its rate cutting cycle this year. This in turn would lift consumer confidence and hopefully boost his popularity.

Tides turning

Recent events appear to have turned the tides for Biden. The escalation of student protests across the United States has underscored the difficulty in toing the line between free speech and incitement. This is unlikely to benefit the Democratic party. President Biden's stance on the Middle East has also angered voters in key swing states such as Michigan. The protests on university campuses will likely encourage the Biden administration to sway key parties in the Middle East to de-escalate the conflict.

Coupled with a challenging political backdrop, the economy has also proven difficult for Biden. Although growth remains resilient, recent data indicates inflation will remain stickier for longer. Many voters blame Biden for high inflation, and these latest figures are unlikely to help him.

Fed meeting

Given the inflationary picture, markets were on edge this week as the Fed met to assess the latest data and share its latest thinking. Crucially, Fed Chairman Jerome Powell quashed any speculation that the next move would be a hike rather than a cut. Beyond this reassuring comment, the Fed's assessment of the latest economic landscape has converged with what investors priced in over April. Investors priced three rate cuts at the end of March. In April, investors moved to price in just one 0.25% rate cut by year-end, pushing bond yields higher and paring back some of equity markets' gains so far this year.

At the start of the year, the Fed emphasised it needed more evidence that it was well on the way to reaching its 2% target inflation rate. But in May, Powell noted progress towards hitting the 2% inflation rate has stalled. This put all previous expectations of a summer rate cut to bed.

As the outlook looks more uncertain, Powell was quite careful to reassert the Fed's data dependency. He shied away from making any concrete policy guidance. Furthermore, the Fed announced that they would slow the pace of its Quantitative Tightening program beginning in June. On the whole, the Fed's actions and words were seen as less hawkish than they could have been, resulting in both bonds and equities recovering after April's drawdowns.

Consumer confidence wanes

The Conference Board Consumer Confidence Index, which measures consumer confidence, declined to its lowest level in two years.[2] The repricing in bond yields has taken 30-year mortgage rates to around 7.5%, up 0.50% from the start of the year,[3] adding to President Biden's problems.

It also creates challenges for the Fed. Over the past decade, the Fed, along with other developed market counterparts, has encountered heightened politicisation on its decision-making process. Ideally, the Fed was hoping to cut rates in June or July to avoid any perception that its decisions were politically motivated. It is a narrative Trump has been sticking to. "I think he's going to do something to probably help the Democrats, you know, I think if he lowers interest rates," Trump said in a February interview with Fox Business, adding that he would not reappoint Powell if he wins in November.[4]

The first interest rate cut is now expected by September or December this year, uncomfortably close to the election. While the economy and inflation are forcing the president and the Fed to bide their time, it is undoubtedly an unwelcome development for the Democrats.

[1] Citizens for Responsibility and Ethics in Washington, https://www.citizensforethics.org/reports-investigations/crew-reports/trumps-91-criminal-charges-and-where-they-stand/

[2] The Conference Board

[3] Bankrate.com

[4] Politico, https://www.politico.com/news/2024/02/02/trump-says-he-would-not-reappoint-political-jay-powell-as-fed-chair-00139311

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