



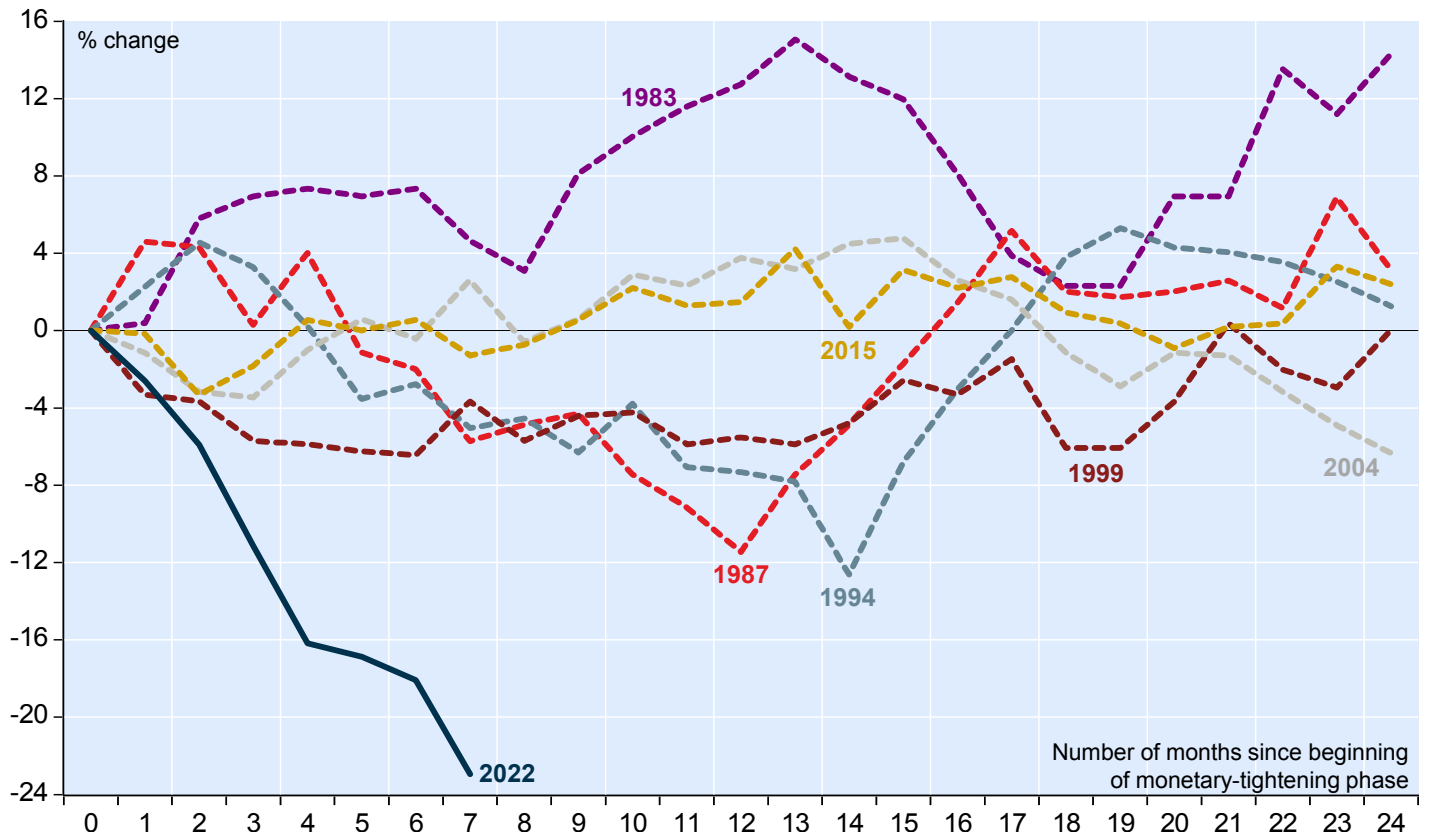
## U.S. Watch

By Jocelyn Paquet

The statement released by the Federal Reserve following its latest monetary policy meeting mentioned that, in determining the pace of future rate increases, the Committee would take into account “the lags with which monetary policy affects economic activity and inflation.” Asked to provide more details on that topic at the press conference which followed the rate announcement, Chairman Jerome Powell stated that, although monetary policy worked with long and variable lags, newer literature suggested transmission times might be shorter today than in the past because movements in financial conditions now happened *ahead* of the central bank’s moves. Powell then said it would be irresponsible for the Fed to ignore this new research but admitted that a great deal of uncertainty remained around the subject of lag times. The whole question may seem academic, but it is of vital importance for the conduct of monetary policy. If transmission times are indeed faster, the impacts of monetary tightening would be felt more quickly and the chances of seeing a de-anchoring of inflation expectations would be lower. This would in turn allow the Fed to stop raising rates sooner. But how will the central bank know? Looking solely at inflation and employment will not help, as these are lagging or coincident indicators. Instead, the Fed should focus on leading indicators. Specifically, it should pay more attention to housing. It’s true that real estate accounts for just a small part of U.S. GDP, but it tends to react faster to changes in interest rates. And boy is it reacting now! As today’s Hot Chart shows, home resales have collapsed since the Fed started raising rates earlier this year and the scale and speed of the decline has had nothing in common with what had been observed in prior tightening cycles. To be sure, transactions have contracted every single month this year (the longest streak in data going back to the 1970s) and now stand at their lowest level in nearly 11 years. And while some commentators are keen on describing this process as a mere return to normal following the pandemic boom, we see it as an indication that monetary policy is more restrictive than would appear, something that is being masked in consumption data by excess savings accumulated during the pandemic.

### U.S.: Housing freeze hints at rapid transmission of monetary tightening

Monthly change in home resales in the two years following the beginning of Fed tightening phases



NBF Economics and Strategy (data from Bloomberg)



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