

Will old habits die hard at the Fed?

By Taylor Schleich, Ethan Currie & Vy Le

The dust has settled after the Fed's first decision under Kevin Warsh, resolving *some* uncertainty. But plenty of questions remain, with policy ambiguity a deliberate feature of this new-look FOMC. That was clear last week when investors received an ultra-slim rate statement with no forward rate guidance. This new communication strategy marks a clear departure from the Powell Fed, which ensured markets knew what to expect by decision day. Case in point: the next Fed meeting is priced as a toss-up (~40% hike odds) and may remain as such right up to July 29th.

Last week, many were also struck by more inflation-focused messaging. That's fully consistent with Warsh's Senate confirmation hearing, which also emphasized price stability over labour markets. Greater concern about inflation was likewise evident in the dot plot: half of the FOMC now expect to deliver at least one hike this year. We don't doubt they *could* follow through on that, but the empirical record argues for skepticism. The June median dot has a sub-50% 'hit rate', and in each of the past three years, the policy rate has ended the year *lower* than the Fed signaled.

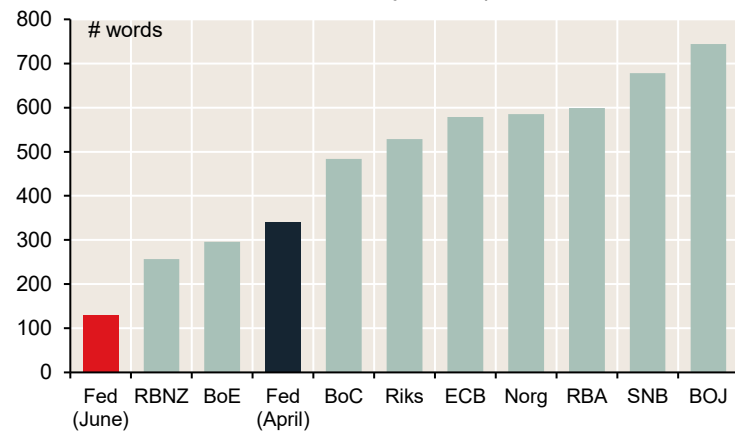
Nonetheless, markets viewed the decision as hawkish. The 2-year UST sell-off on Fed day was the 6th largest since 2000. Typically, front-end

weakness extends out the curve too but this time, 30-year yields ended the day *lower* (helped by an ongoing pullback in term premia as Middle East risks faded). We understand the logic: political independence and a tougher inflation stance support the long end. But if the conclusion is that Warsh is staying true to his beliefs, is it reasonable to expect a balance sheet 'task force' will offer anything reassuring for long-term Treasuries?

The curve will also depend on whether this apparent hawkish shift is reinforced with hikes or is just rhetorical. If the central bank really wanted to prove it was laser-focused on price stability, a hike next month would make that clear (and Thursday's PCE data won't argue against such a move). But while that is a real and legitimate possibility, we're skeptical. Instead, we expect many officials will balk at starting a new hiking cycle right when inflation begins easing (which it will start to do in June) and with inflation expectations that aren't all that alarming. Warsh may be positioning this as a new Fed—and in many ways, it is—but there are 18 other officials from a bygone era. For them, this kind of inflation outlook has been good enough to not only avoid hiking, but to bring rates closer to neutral. We may soon be reminded that old habits die hard... but the debate itself shows the Chair has markets right where he wants them.

Chart 1: The Fed's *already* lean rate statement got leaner

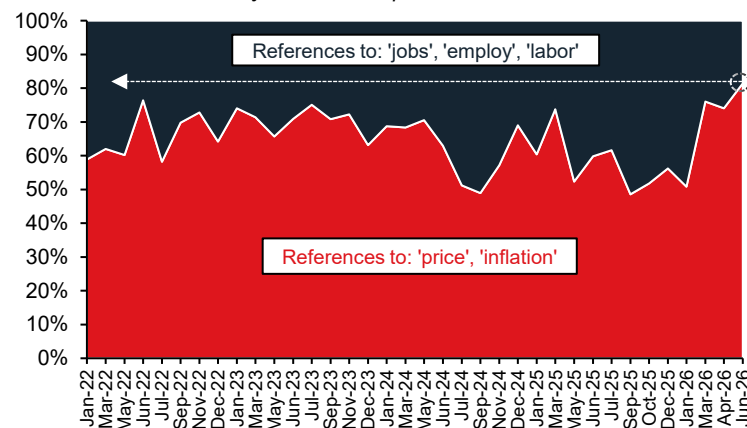
Word count in latest rate statement for major developed market central banks



Source: NBC, various central banks

Chart 3: Warsh's first presser skewed toward inflation ...

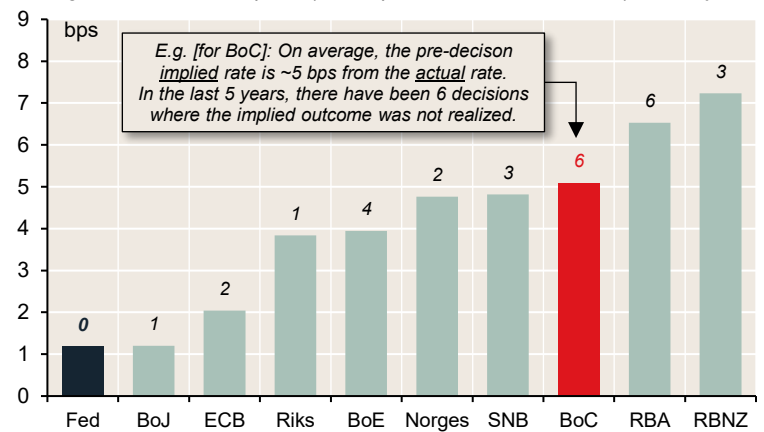
References to mandate objectives in Fed press conferences since 2022



Source: NBC, FRB | Note: Word count includes questions posed to Powell/Warsh

Chart 2: The Fed was the most predictable central bank

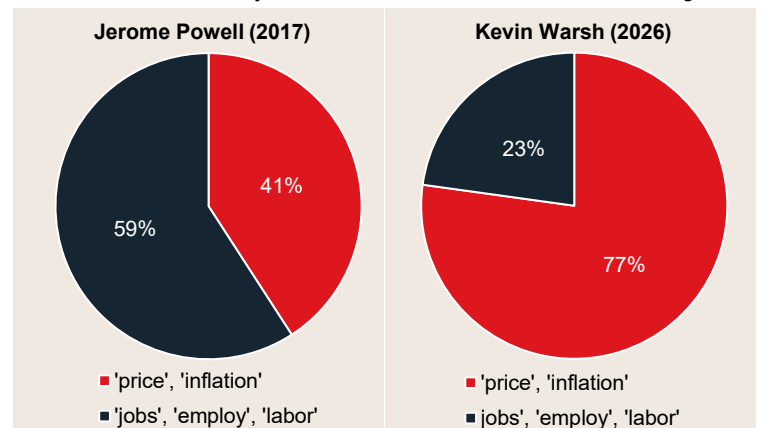
Average absolute OIS 'surprise' (what's priced vs. what's delivered): Last 5 years



Source: NBC, Bloomberg | Note: Labels denote number of 'surprises' in last 5 years

Chart 4: ...just as his confirmation hearing did

References to mandate objectives in Powell & Warsh confirmation hearings

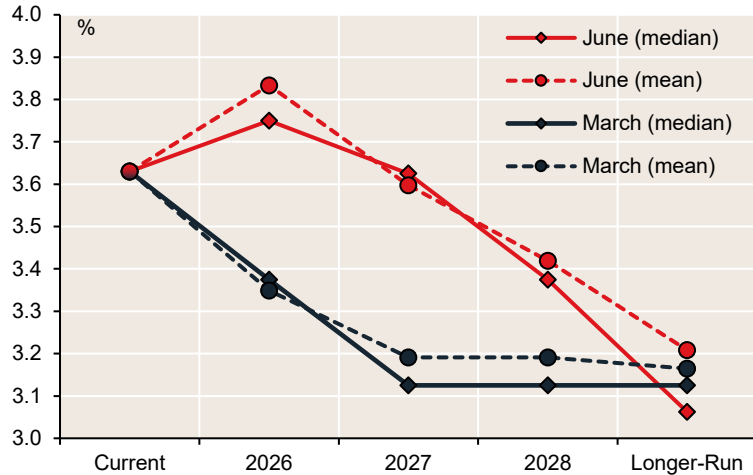


Source: NBC, US Senate | Note: Word count includes Senator questions & nominee responses



Chart 5: An apparent hawkish shift at the Fed

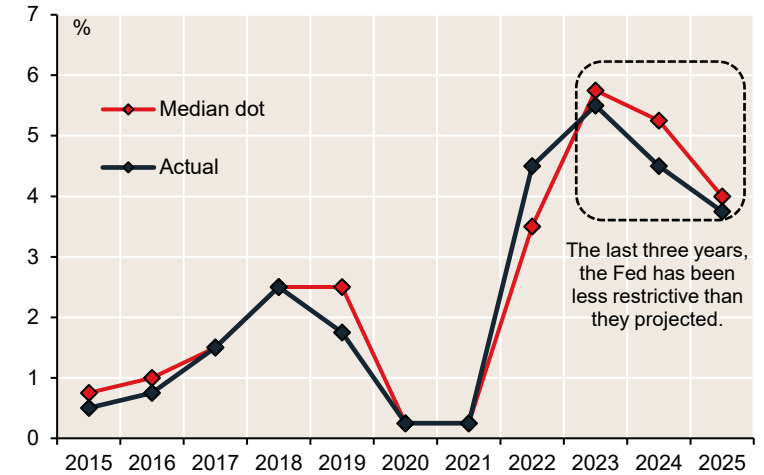
Median and mean fed funds projection: March 2026 vs. June 2026



Source: NBC, FRB

Chart 6: Doubt the dots? Empirically, there's reason to

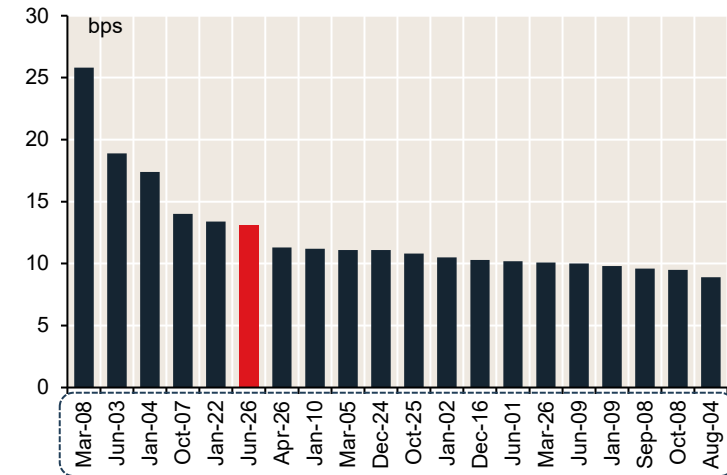
Median dot each June and actual end-of-year policy rate target



Source: NBC, FRB | Note : Median dot adjusted to upper bound of target range.

Chart 7: Warsh produced a large front-end repricing...

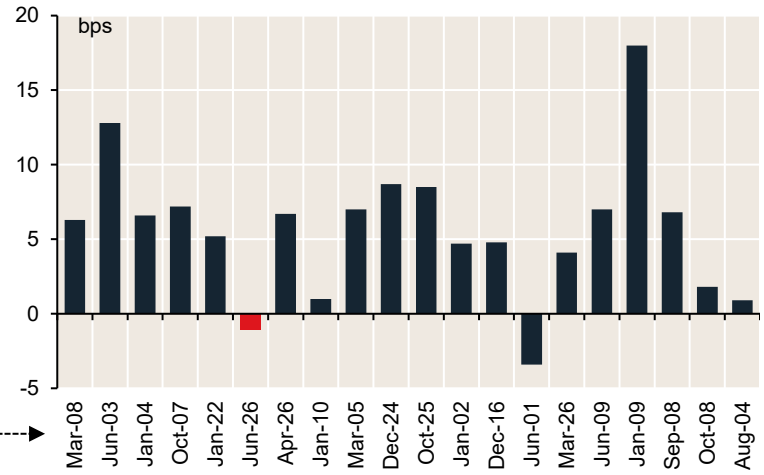
25 largest 2-year yield increases on Fed decision days since 2000



Source: NBC, Bloomberg

Chart 8: ...but the long-end didn't follow suit

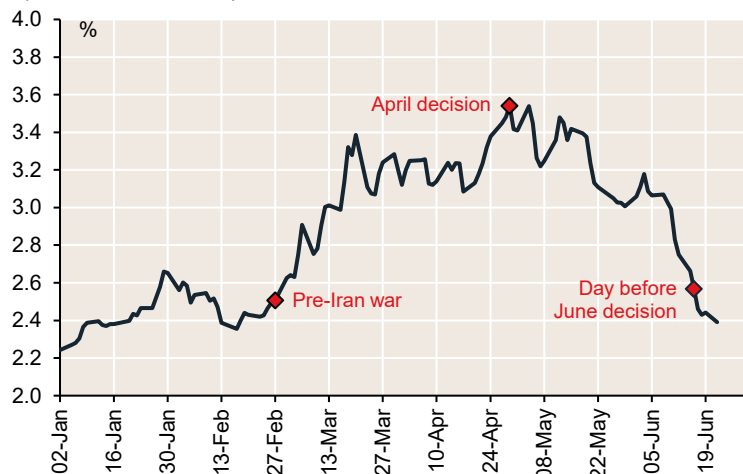
Change in 30-year yield on Fed days that the 2Y yield increased most (see left)



Source: NBC, Bloomberg | Note: Covers all meetings since 2000.

Chart 9: Inflation risks easing, even before hawkish Fed

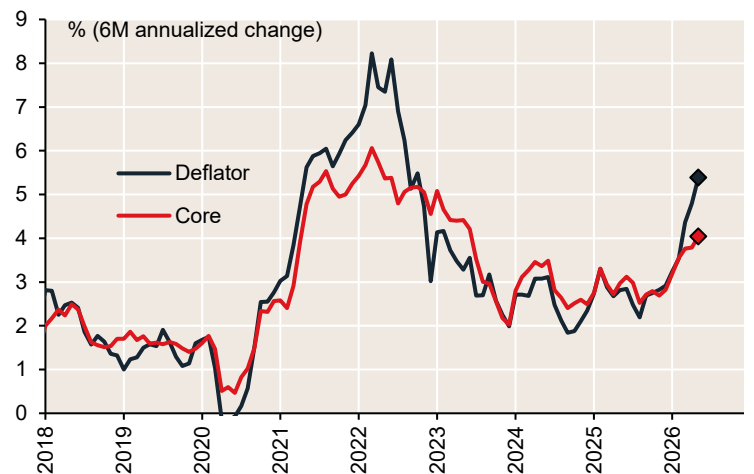
1-year U.S. inflation swap in 2026



Source: NBC, Bloomberg

Chart 10: A hike could be justified based on May inflation

U.S. PCE inflation: Headline and core on a 6M annualized basis



Source: NBC, Bloomberg | Note: Using May BBG consensus M/M forecast for last point



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