# Month in Cash: Neutral November

**11-30-2018**
The buzzwords in November for cash managers were not “market volatility,” but “neutral rate.” Vice Chair Richard Clarida discussed it and Chair Powell made it a focus of public comments. Of course, Fed economists and officials view a neutral rate of interest, the level at which the economy doesn’t need stimulus or tightening, as a central policy concept. Some even give it a number: 2.9%, making it seem a precisely calculated point. But there’s nothing magical about 2.9%, and ultimately it is more confusing than helpful, especially when the head of the central bank waffles on it.

In early October, Powell said that interest rates were “a long way from neutral.” Only a few weeks later, in his speech Wednesday at the Economic Club of New York, he said rates were “just below” that level. The markets were indeed volatile during that span, but economic data hardly changed, so perhaps his view of equalibrium has.

Powell’s shifting stance is almost certainly not going to stop the Fed from raising rates 25 basis points to a 2.25-2.50% federal funds target range in its policy-making meeting later this month, as the increase is all but fully expected by the markets. The takeaway probably will be that the policymakers intimate only two hikes in 2019 instead of three. We also continue to expect the neutral rate will be reached in the first half of 2019. Until that time it is normalizing—or dare we say neutralizing—rates, not tightening them. And that is a point often lost in the discussion and debate on monetary policy: the Fed isn’t obligated to stop at neutral. If it still feels that the economy is overheating and causing inflationary pressures, it will push right past that. And if policymakers think the economy is slowing but inflation is growing, they will react to inflation.

It remains to be seen if the Fed addresses its plan for quantitative tightening at the meeting. We anticipate it to continue rolling off $50 billion of securities a month. The focus will be on the dots, which come with the statement in December. As for what those dots may indicate, we offer this suggestion: perhaps the Fed should leave neutral to electric wires and car transmissions.

In November, the London interbank offered rate (Libor) steepened over the course of month ahead of the likely December move. One-month rose from 2.30% to 2.35%, 3-month from 2.52% to 2.74% and 6-month from 2.78% to 2.89%. The weighted average maturity (WAM) target ranges of our funds were unchanged in November, with prime and municipal funds in a 30-40 day span and government funds in a 25-35 day range.

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