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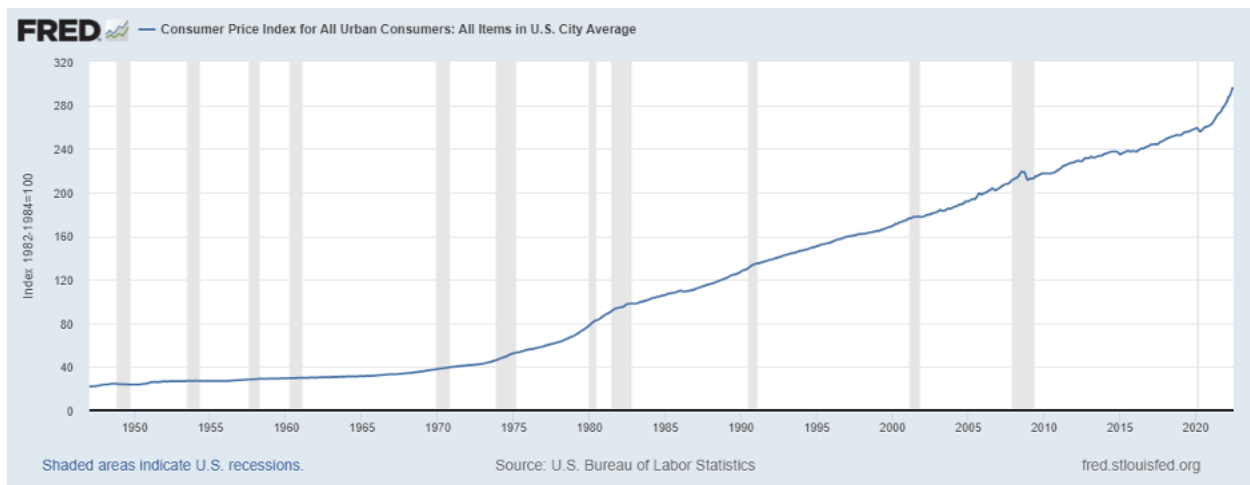
Will The Fed Be Like Mike Tyson Or Floyd Mayweather?

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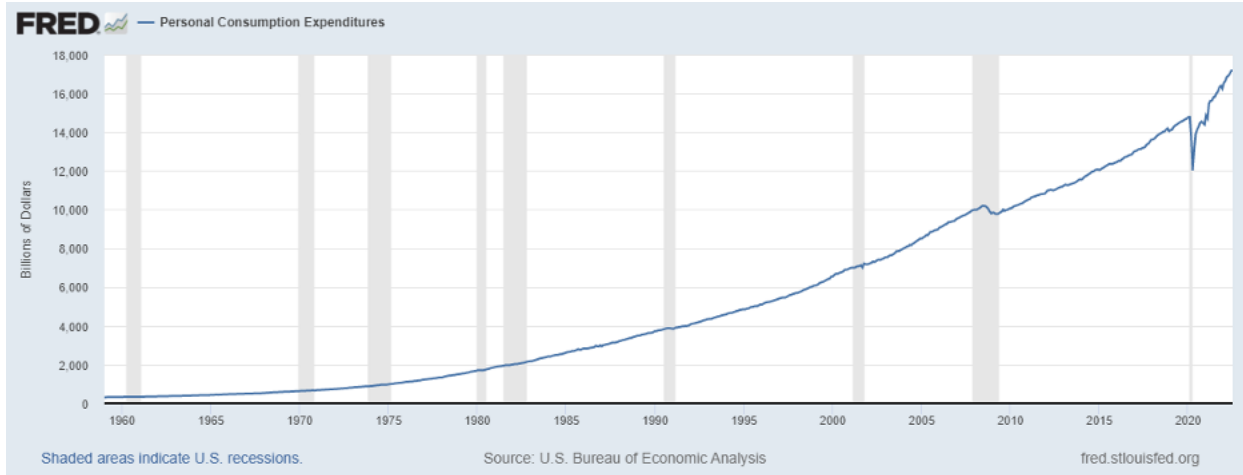
September 16, 2022

Sports analogies can be confusing, depending on the audience, but when discussing inflation, terms that could be considered derivative of sports are thrown around rather frequently.

So, in the theme of sports etymology, what strategy will the U.S. Federal Reserve and its Federal Open Markets Committee (FOMC) use to knock out inflation and leave it flat on its back? Market participants discuss "peak inflation," but it's important to note that inflation (as measured by the Consumer Price Index or Personal Consumption Expenditures price index) is an index continually rising, give or take the occasional recessionary/deflationary periods.



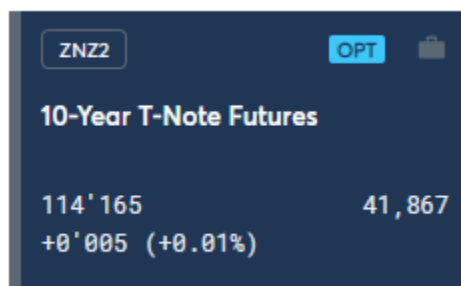
U.S. Bureau of Economic Analysis, FRED



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When the discussion is around "peak inflation," market participants reference the second derivative, or the rate of change of inflation. Has the rise in inflation slowed, flattened out or even fallen is the question being raised when the debate centers on peak inflation.

In simpler terms, inflation is a foe that keeps coming, and slowing down inflation has to be taken very seriously. Jerome Powell and other members of the FOMC have been out in full force, repeatedly saying precisely this – that they will fight inflation with focus and aggressive action. As Powell said this month at the Cato Institute's 40th Annual Monetary Conference, "The Fed has, and accepts, responsibility for price stability." He added, "We need to act right now – forthrightly, strongly."



Source: CME Group

Mike Tyson or Floyd Mayweather?

The Fed is committed to the fight against high inflation, but to put this in terms of a sports analogy, will it fight like Mike Tyson or more like Floyd Mayweather?

You would likely know these two names even if you are just a casual fan of boxing. Mike Tyson was the youngest heavyweight champion in boxing history and a feared power puncher. He won his first 19 professional fights by knockout, with 12 knockouts taking place in just the first round. When the FOMC first hiked rates 75 basis points in June and then hiked rates again in

July by another 75 basis points, an observer might think that the FOMC was trying to knock inflation out in the first round.

Then the talk of a "pivot" started, and while that's not exclusively a sports term, it is used frequently in sports to reference the footwork of an athlete. In boxing, a pivot is when the boxer's front foot remains planted and works as a point of rotation, while the back foot swings around in a half circle so that the fighter is now facing the other way. It is used mainly as a defensive maneuver to avoid a punch and set up the next set of counterpunches.

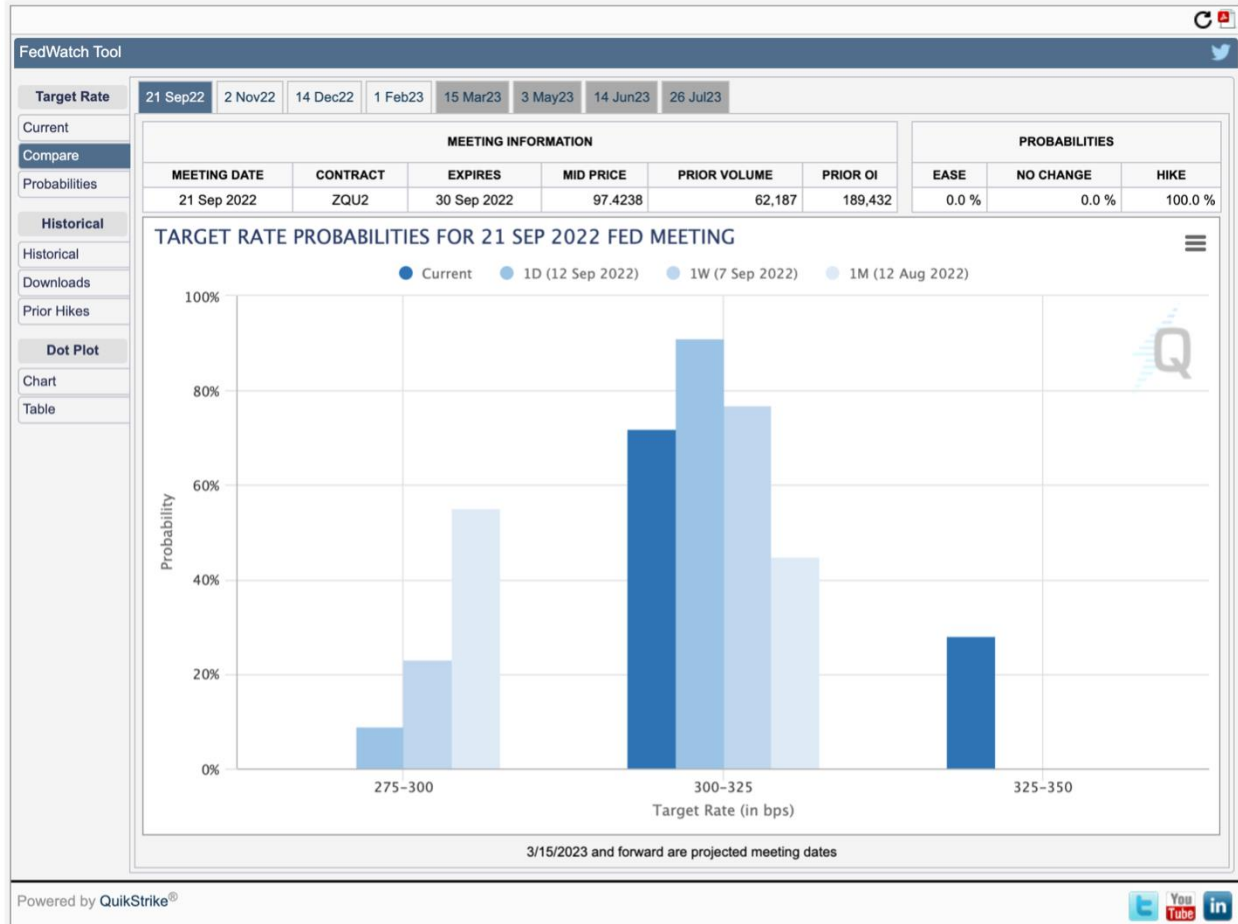
One of the masters of the pivot was Floyd Mayweather. Floyd Mayweather's boxing career ran from 1996 to 2017, when he retired with an undefeated record. Mayweather won 15 major world championships across five different weight classes. He was not, however, known as a big puncher. He won only 27 out of his 50 fights by knockout and was best known for his defensive abilities, fast hands, footwork – and his pivot.

A 'Mike Tyson' Fed would continue to hit the market with outsized rate hikes. The Fed is currently raising interest rates at its fastest pace in four decades, and is trying to knock its primary foe flat on its back as early in this fight as possible, at least so far.

On the other hand, a 'Floyd Mayweather' Fed would likely pivot after a few hard punches and manage its remaining energy with defense and smaller counterpunches.

What's Next for the FOMC?

As we approach the Sept. 20-21 meeting of the FOMC, the speculation on the size of the next rate hike will dominate the headlines more and more. Glancing at the [CME FedWatch Tool](#) under the 'Compare' tab, you can see that since Aug. 9, the probability is toward the Fed acting more like Mike Tyson (the probability of a 75 bps rate hike has climbed from an early September low of 57% to 72% currently).



Source: CME Group

The risk of the Mike Tyson approach is that the Fed uses too much energy initially and ends up hurting its credibility by potentially driving the U.S. economy into a severe recession. On the other hand, the risk of the Floyd Mayweather approach is that inflation enters the ring with surprising stamina and outlasts the lighter punches, driving the U.S. economy into a sustained period of stagflation.

Whichever path the FOMC takes, they will be questioned and likely blamed for any adverse outcomes. One thing is without question, though; you can't step into a ring against a foe like inflation and expect not to take a punch.