Cato's Poole: Fed's December Statement a 'Policy Communications Failure'

By Dan Weil

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The fact that the stock market rose in response to the Federal Reserve's policy statement last month stating that it would be "patient" in raising interest rates wasn't a good thing, says William Poole, a senior fellow at the Cato Institute and former president of the St. Louis Fed.

"Is a positive surprise a positive omen?" he asks in a guest commentary for **Forbes**. "No, it is, instead, evidence of policy communications failure. I suspect (but do not know) that the Fed leadership did not intend to deliver a positive surprise."

Fed Chair Janet Yellen emphasized in her press conference that substitution of the word "patient" for "considerable time" wasn't meant as a policy change.

But, "the market probably reacted less to any particular wording in the statement than to its overall tone of not yet" for interest rate hikes, Poole says.

So while the Fed may have surprised the market inadvertently, that's "no more an advertisement for orderly policy than is a deliberate surprise," Poole says.

"Stable policy requires that two conditions be met. One is that the economy behaves as the Federal Reserve expects. How can the Fed know what to do if this condition is not met? Second, the Federal Reserve must behave as the market expects. How can markets, of all types, determine sensible prices if this condition is not met?" he asks.

"The surge in equity prices shows that these two conditions are far from met. The Fed is making a huge mistake by continuing to treat the economy as if it is in a fragile state. It is not. Anyone who follows the data can count the ways."

Meanwhile, **Wall Street Journal columnist Spencer Jakab** says that the Fed's "'patient' stance on raising interest rates may ultimately cause trouble for the stock market.

"Corporate profits face a potential triple whammy," he writes.

First, foreign money is flowing like wine into Treasurys. That in turn has boosted the dollar. And "with more than 40 percent of S&P 500 revenue earned abroad, dollar strength will pinch sales and margins," Jakab says.

"Meanwhile, the shrinking spread between short and long [interest] rates may squeeze profits of U.S. financial firms. Finally, the reason foreign central banks are out of sync with the Fed is that their economies are flirting with recession and even deflation — hardly good news."