

April 29, 2026

### **Powell's Final Grade: B-**

We eagerly await explanations from the three FOMC member who dissented with the inclusion of an “easing bias” in the April FOMC statement. The statement does not contain any explicit bias, only the continuation of language about “additional adjustments” that in the past has referred to potential rate cuts. We suspect that the dissenters wanted clear language mentioning a potential rate hike if inflation remains higher than expected. Chairman Powell thus leaves an unusually divided Fed. There have not been four dissents, including Stephen Miran’s vote to cut by 25 bps, since 1992. The Fed is not going to move until data comes in to move the Fed away from its December forecast for 2.6% y/y core-PCE inflation and 4.4% unemployment.

What will it take for the Fed to cut again in 2026? We see three scenarios. **The first is a rise in the unemployment level to its recent high of 4.6%**, assuming that there are no data issues (such as a higher labor force participation rate) that make such an increase illusionary. We expect this to occur by autumn, and **we now expect a rate cut in October (we previously expected September)**. The second would be for core-inflation to exhibit three to four months of subdued readings. As we discuss later, we expect following hotter readings through May, core-inflation will decline this fall. The third is a full reversal in energy prices, likely due to an unexpected decline in tensions in the Middle East. We do not expect this until 2027.

Given that nine FOMC members, including Miran, supported the continuation of an easing bias, and given Kevin Warsh’s preference for rate cuts, **the bar for a rate hike is very high and the odds of one are less than 10%**. The connection between energy prices and core-inflation, which has been very weak since the 1980s, would have to reappear. **It would take a combination of core-inflation readings over 3% and significantly higher 3-5 year ahead inflationary expectations, to persuade the Warsh Fed to raise rates this year.**

Chairman Powell’s somewhat surprising decision to remain as a Fed Governor after Kevin Warsh takes over, does not affect our outlook. Given his comments that he had “planned on retiring” but for the ongoing criminal investigation of cost overruns into the Fed’s new building, we expect this investigation to quickly conclude. That will allow Powell to retire within a couple of months and President Trump to appoint another FOMC member.

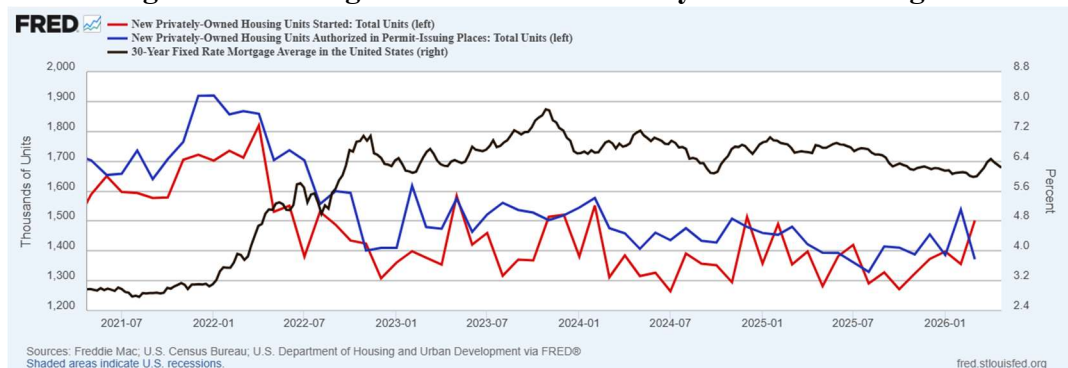
### **Other Developments in Macroeconomics:**

1. **With April being Chairman Powell’s last meeting as Fed Chairman, we grade his tenure as a B-, competent but with serious flaws.** Powell’s Fed usually made the right decision, but often six to nine months too late. Reckless fiscal policy deserves the most

blame for the inflation surge of 2021, but Powell made two mistakes that made the problem significantly worse. First, he promised to keep rates near zero under the labor market returned to maximum employment. Second, he misread inflation in 2021 as entirely transitory. **Under Kevin Warsh, the Fed is more likely to make the opposite mistake by failing to respond aggressively enough to weak growth or higher unemployment.** Given his prior comments on non-conventional monetary policy, Warsh will struggle to respond to a severe recession where lowering the Federal Funds rate to near zero is not enough.

2. The March housing data are interesting because they are the last report before the current spike in mortgage rates will have an impact. The 10.8% m/m increase in housing starts (red in Figure 1) is far less impressive than it appears given that permits (blue in Figure 1) coincidentally fell by the same amount in March. Historically, these two series are equally informative, and the March data are partly just a reversal of February when starts were weak, but permits were strong. Overall, both series have shown a disappointingly weak upward trend since June 2025 when mortgage rates (black in Figure 1) began a long decline that only ended with the outbreak of the Iran conflict in June. With the 30-year average fixed mortgage rate up from 6.00% in early March to 6.23% today, upcoming housing data will be weaker. Given that housing remains our favorite leading economic indicator, this is bad news for 2Q2026 growth.

**Figure 1: Housing Starts and Permits May be Set to Fall Again**



3. Our continuing bullishness on lower yields is grounded by evidence suggesting that neutral (and the Fed's likely landing spot in 2027) is much lower than the 370 bps that bond markets expect. We still put neutral at just below 300 bps. The interesting part of the ongoing surge in yields from the Iran war is that they are entirely driven by expectations that the Fed will remain higher for longer. After briefly rising a few weeks ago, term premiums are back down to their February levels. **Financial markets are overreacting to the Iran war's impact on oil prices.** We reiterate that the bulk of the inflationary impact has already been passed on to headline inflation. While core-inflation reading will

also uptick through May or June, this process will be finished by 2H2026. **We continue to expect inflation to ease enough by October for Warsh to enact his first rate cut.** This will begin a process lowering the Fed Funds rate to 250-275 bps and the ten year Treasury yield to 340 bps by mid-2027.

-Paul Shea

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