

# All you need to know about the Fed and how to profit from anticipating its policy actions

In *Fed Watching for Fun and Profit*, economist Edward Yardeni delves into the history of the institution and its internal workings, so as to enable investors to understand its decision-making process.

BY SHRAVAN KUMAR SREENIVASULA

**F**ED *Watching for Fun and Profit: A Primer for Investors* provides a detailed explanation of a topic that economist Edward Yardeni discussed in *Predicting the Markets: A Professional Autobiography*. His lessons from following and analysing the Federal Reserve Board over several decades are encapsulated in a few hundred pages.

Those who have read *Predicting the Markets* should be familiar with his narrative style, which instructs readers in a simple, straightforward manner.

Yardeni covers all aspects of the Fed, from its beginnings in 1913 to the present day. He details the transformations that the institution has undergone in terms of its structure, its mandate, and the individuals heading it. Yardeni also explains how the Federal Open Market Committee (FOMC) gets constituted, how its meetings proceed, who votes, what data get looked at, and how the resulting policy statement is disseminated.

The author emphasises the importance of identifying who is powerful within the FOMC, how they influence public opinion, and how the Fed policy statement should be read and evaluated in divining the future direction of interest rates.

On the matter of carefully interpreting the policy statement, consider what happened in the last quarter of 2018. By dropping the two

words “accommodative stance”, the September 2018 statement created inconsistent communication regarding the FOMC members’ future expectations. Investors inferred that rate tightening was in store and consequently knocked 20 per cent off the major stock indexes’ value in less than two months.

The markets calmed down after Fed chair Jerome Powell executed his now-famous “Powell pivot” by committing the Fed to be “patient” in raising rates.

## Last five Fed chairs

*Fed Watching for Fun and Profit* profiles in detail the last five Fed chairs and describes their thought processes before and after assuming the post. Yardeni explains how philosophy, context, and personal belief systems affect the decision-making process. These are unique to each Fed chair. For example, Ben Bernanke acted as he did during the Global Financial Crisis (GFC) because of his understanding of what occurred during the Great Depression. The United States and the world could have gone on a different path if someone else had been the chair during the GFC.

Yardeni helpfully takes readers through a number of important historical events. Among them are the dissolution of the Bretton Woods system, the International Monetary Fund (IMF)’s dollar rescue package, the switch in monetary policy target-



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ing from the federal funds rate to money supply, and the Fed’s response to market crashes by rescuing banks and bailing out a variety of firms.

The book contains a wealth of fascinating trivia. For instance, it is pure serendipity that Jackson Hole, Wyoming, has become the permanent destination for the Fed’s annual economic symposium. This event is attended by central bankers, finance ministers, academics, and leading market participants from around the world.

The frequently underrated Smoot-Hawley Tariff Act of 1930 helped transform an ordinary recession into the Great Depression. At

Yale University, graduate students still use a past Fed chair’s class notes as an unofficial textbook. One Fed chair received a presidential request to resign but refused to do so, despite intense pressure. A person once entered the Fed building with the intention of taking the Federal Reserve Board members hostage.

## Lenders of last resort

The author shows how investors can take profitable positions by anticipating how the Fed will act. Portfolio managers who read this book probably would have positioned themselves to benefit from the rebound of risky asset classes during the Covid-19 correction in 2020.

Yardeni stresses that for the past

300 years central banks have acted as lenders of last resort and argues that they will continue to do so. He makes it clear that there is no point in fighting or second-guessing the Fed, regardless of one’s own ideas regarding appropriate monetary policy.

The author briefly touches on unconventional tools that the Fed might use in the future. One example is the Treasury’s special account with the central bank, which can be filled in pursuit of employment and inflation objectives. On another timely matter, Yardeni expresses his doubt that governments and central banks will allow cryptocurrencies to take over the monetary system.

In summary, *Fed Watching for Fun and Profit* is a crash course for anyone interested in monetary policy actions, financial markets, and the economy in general. Institutional investors, individual investors, businesspeople, policymakers, and students can gain from it a solid understanding of how the Fed has acted in the past. This knowledge can help decision makers predict the Fed’s future actions and their associated economic and financial market impacts and determine the actions that accordingly need to be taken.

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