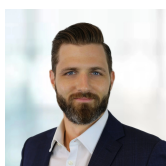


THE WARSH DOCTRINE: LESS GUIDANCE, MORE MARKET (AND WHAT THIS COULD MEAN FOR THE COINS)



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First Reaction to FOMC: The headline takeaway from this meeting is hawkish, but the more important story may be the Fed's evolving framework. Warsh appears intent on reducing forward guidance and placing greater weight on market prices and real-time economic data. Notably, 2-year yields are rising while 2-year inflation swaps are falling, suggesting that higher rates are increasingly reflecting real growth expectations rather than inflation fears. That keeps the Fed hawkish today, but if market indicators of inflation expectations continue to improve, it could eventually create the conditions for a more dovish policy response later in 2H. Near term, that is a headwind for crypto as the market adjusts. Medium term, it remains one of the more constructive developments to monitor. Below are more in-depth takeaways.

Unequivocally Hawkish SEP – The June Summary of Economic Projections was about as hawkish as one could expect. The dot plot reflected a median expectation from the FOMC of one rate hike this calendar year, slightly above market pricing heading into the event. Half of the projections (9 out of 18, Warsh did not submit projections) forecasted rate hikes, with 6 of those members advocating for multiple hikes. Forecasts for near-term real growth were revised lower, the unemployment outlook was revised marginally lower, headline inflation expectations were revised considerably higher in the near term, while core PCE was forecasted to be significantly more elevated through next year. It is tough to view this as anything but hawkish. Such an SEP was certainly priced in to some degree, but based on market reaction post-press conference (2Y +15 bps, 10Y +6 bps, risk assets lower), it would seem that these expectations, coupled with the comments at the press conference, were slightly more hawkish than had been priced in.

Hawkish Press Conference if Taken at Face Value – The character of this press conference was remarkably different from what the market has been accustomed to. Warsh was short in many of his answers and deferred to the statement and SEP on questions related to forward guidance (more on this below). There were no comments about slack in the labor market, and there were no comments related to the transitory nature of supply-side inflation. He repeatedly affirmed his mandate as Fed Chair ("price stability"), noted that "inflation is a choice," and stated that the Fed is "unanimous and unambiguous" in its mission.

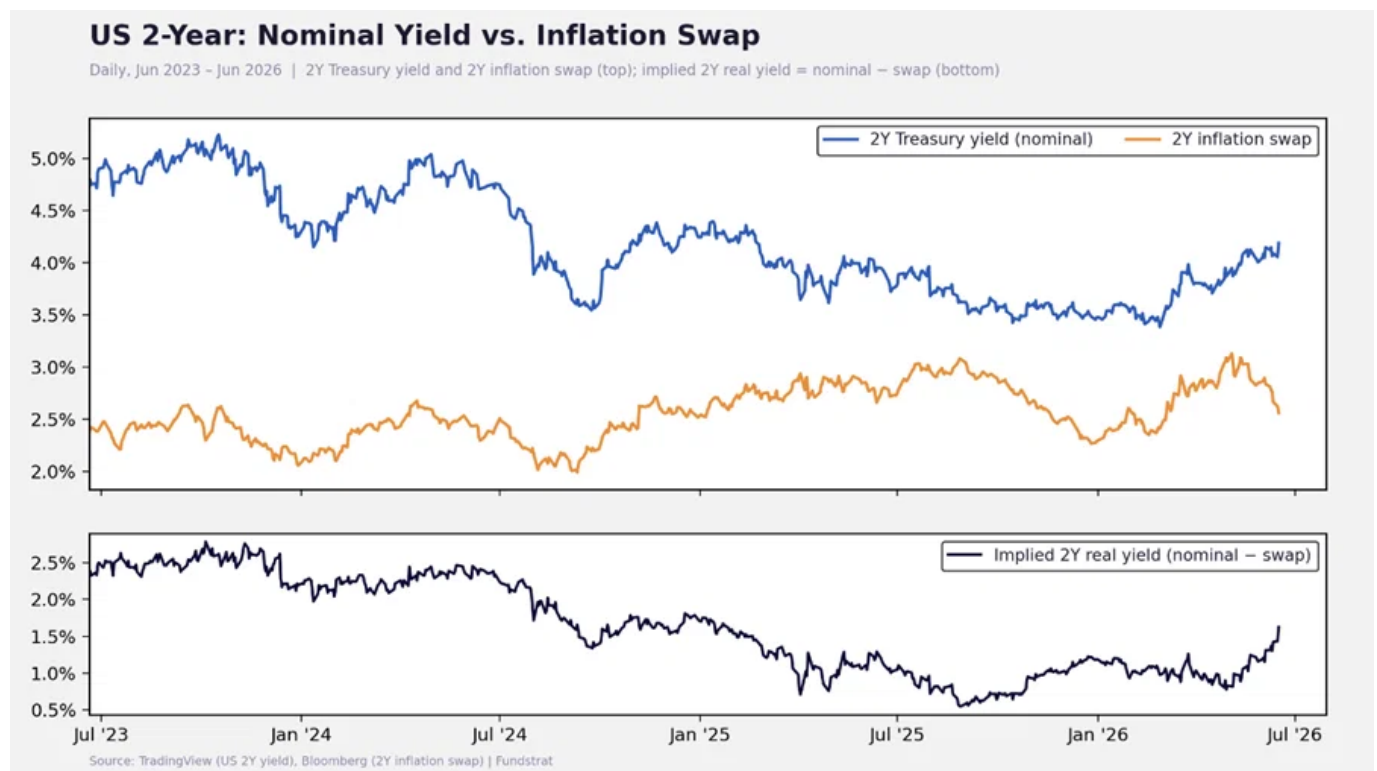
Reduced Forward Guidance – Warsh had signaled prior to his tenure as Fed Chair that he was not a fan of forward guidance. This is a big change for the market, as investors have become accustomed to a pretty constant deluge of information and opinions from both the Chair and the broader Fed. I think reducing forward guidance makes a lot of sense. The concept was introduced in the post-GFC period to quell market concerns about the ongoing crisis of confidence in financial markets. The environment today certainly does not reflect a similar magnitude of uncertainty or panic. It also makes sense to remove policy signaling from the Fed's playbook, as this intuitively pulls easing/tightening effects forward and, in many ways, alters forward-looking data, which complicates the implementation of monetary policy. I suspect that this was, in fact, why Bernanke introduced the concept in the first place. He wanted the market to price in indefinitely accommodative monetary policy in the wake of the GFC. This is no longer necessary. Warsh's first act of defiance was to refuse to provide economic projections. He went on to defer on virtually all questions related to the Fed's forward-looking views.

The Reliance on Market Data and Alternative Datasets – In addition to his reforms on forward guidance, Warsh noted that "financial market prices are probably the most important source of information to guide central bankers. But when all the financial markets are doing is reflecting back what we've said... we're being blind to it." This aligns with my thoughts on forward guidance noted above. Forward guidance, in many ways, distorts the market's interpretation of the actual economy and can affect economic data in and of itself. The point here is that, going forward, the market will pay closer attention to economic data releases and, importantly, will tell the Fed what it should do, as opposed to engaging in a two-way dialogue (i.e., if the 2Y is above the Fed Funds rate, then the Fed should maintain a more hawkish posture).

The key will be determining which economic data Warsh favors. He made a point of stressing that he is not a fan of many traditional economic indicators, especially those that rely on survey data. These measures are antiquated due to their relatively unsophisticated approach to data collection and are often lagging in their ability to forecast the trajectory of inflation, labor markets, and the economy. He specifically

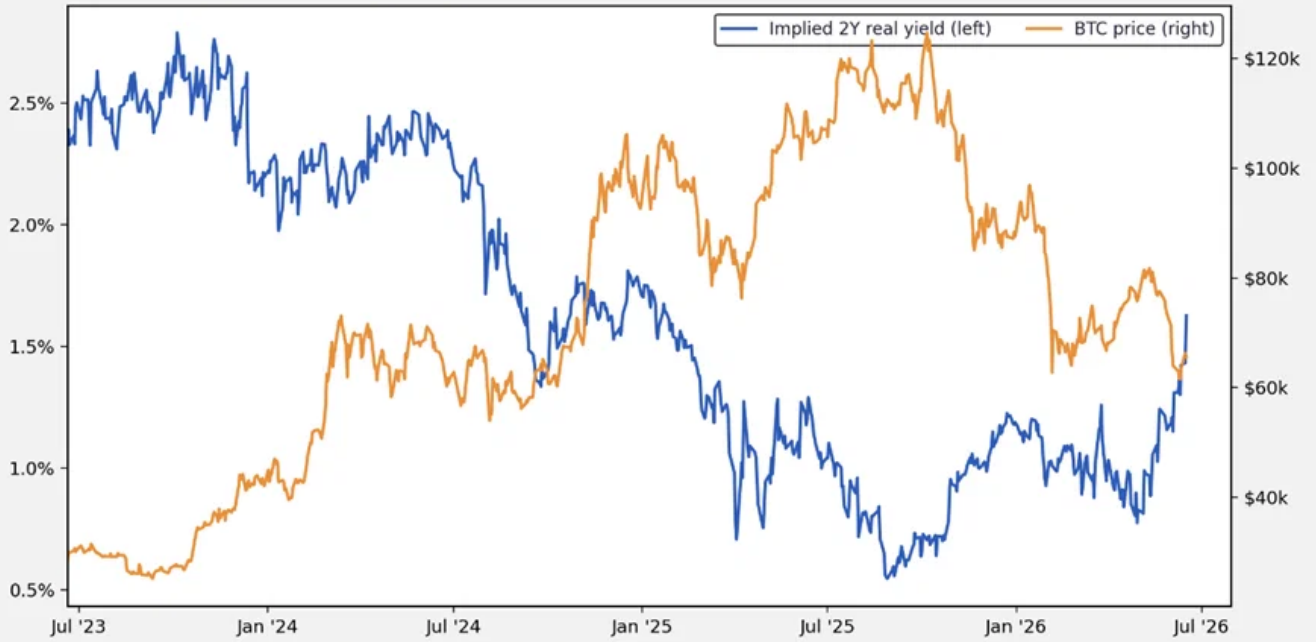
noted that he prefers private-sector data that is more robust and real-time (i.e., ADP versus NFP).

In terms of looking for bullish takeaways amidst what was unequivocally a hawkish output from the Fed, I think this is it. Right now, the 2Y yield is rising while 2Y inflation swaps are moderating alongside a commodity complex that is showing signs of relief. This suggests that the rise in yields is being driven by real growth rather than inflation. Based on this data, should incoming economic releases begin to show signs of inflation abating, it could set the stage for incrementally more dovish monetary policy at some point in 2H, which, as discussed recently, could eventually become a tailwind for crypto.



BTC Price vs. Implied 2-Year Real Yield

Daily, Jun 2023 - Jun 2026 | 2Y real yield = 2Y Treasury yield - 2Y inflation swap (CPI), Corr (levels) = -0.81



Source: TradingView (BTC, US 2Y yield), Bloomberg (2Y inflation swap) | Fundstrat

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