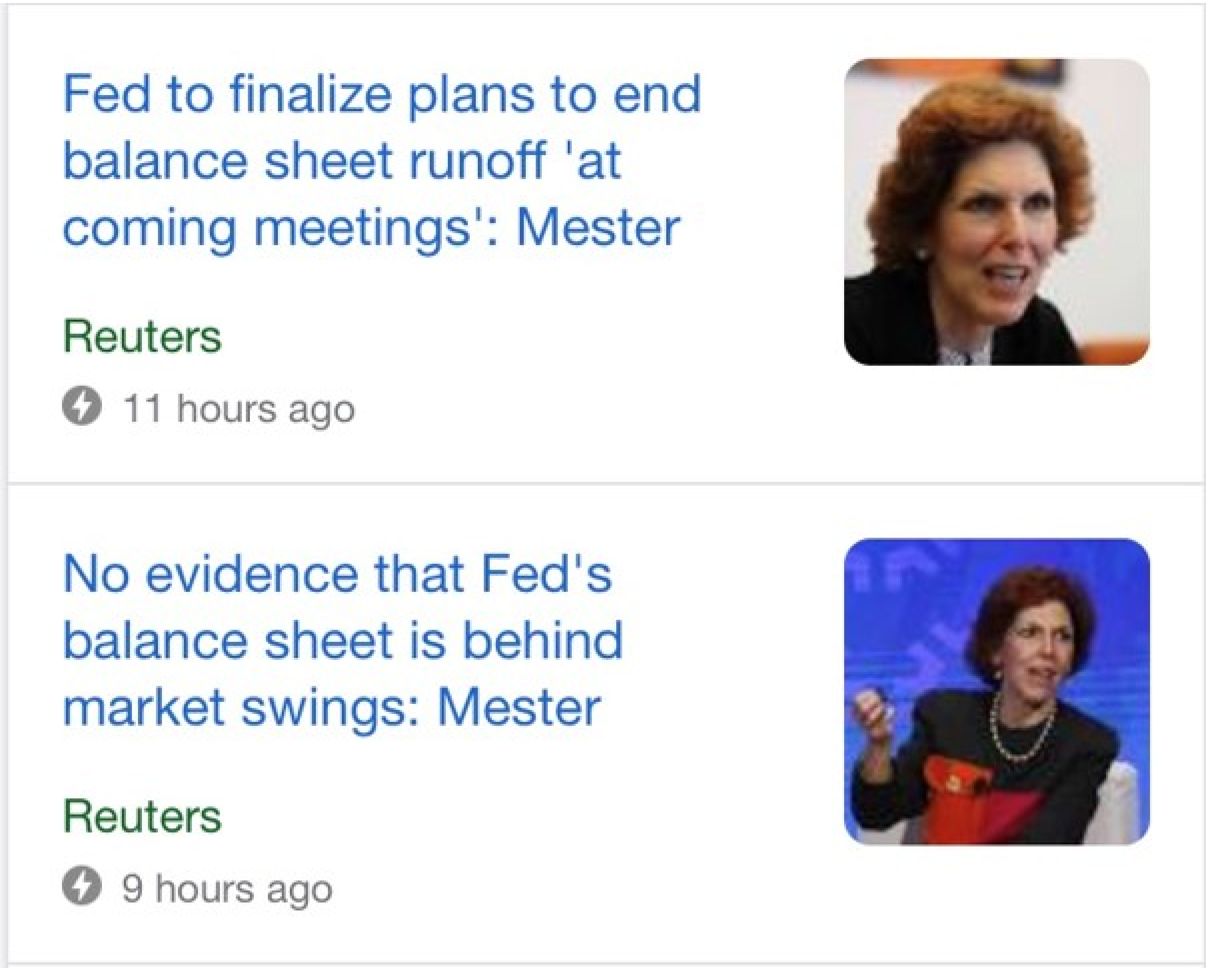
Last night the following Reuters headlines hit the wires. The report is from a speech given by Cleveland Federal Reserve Governor Loretta Mester.



Mester?s comments and similar remarks from other Fed Governors occur within two weeks of a very strong BLS employment report. Over the last two months payrolls have increased by 526,000 jobs, a pace greater than any two month period since July of 2016. Providing further evidence of a strong jobs market, yesterday the BLS released the JOLTS (Job Openings and Labor Turnover Summary) report which confirmed the labor situation is not only healthy but at some of the strongest levels in recent history.

Here are the facts:

- The unemployment rate is only 0.3% above the lowest level in nearly 50 years
- Jobless claims are at levels last seen in 1969
- JOLTS just reported the highest number of job openings since they began reporting on the data in 2000.•

These and other signs of a strong labor market point to the growing possibility that wages, and with it inflation, will rise in the coming months.

Maximizing employment is one of• two Federal Reserve congressionally chartered mandates. The second is stable prices and moderate long term interest rates. Inflation is stable and interest rates are among the lowest in recorded history. The BLS reported this morning that the Fed?s preferred measure of CPI inflation, Core CPI (CPI less food and energy) is running at a 2.2% annual rate. The Fed considers stable inflation to be 2.0%.

To be fair, not everything is rosy. Slowing global growth, further dollar strength, and the ongoing trade debate pose the potential to hamper US economic growth.

Bottom line: there are some clouds gathering on the global economic horizon, but the sun is still shining brightly in the U.S.

With that backdrop, we come back to the question we asked in two articles published two weeks ago. On January 30th and February 1st, we summarized and commented on the recent Federal Reserve FOMC policy meeting. Of importance, we were trying to figure out why the Fed made such an abrupt policy U-turn from the prior meeting on December 19, 2018. Here are the articles.

Quick Take: January 30, 2019 Fed Meeting

Additional Thoughts: Quick Take January 30, 2019 Fed Meeting

Our initial take was that the 20% stock market decline was to blame for the change in policy. It didn?t help that President Trump was calling for Fed action and at the time Powell?s head seemingly daily. In the ?Additional Thoughts? article we posited the following:

> ***What Does the Fed Know?***
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> *During the press conference, the Chairman was asked what has transpired since the last meeting on December 19, 2019, to warrant such an abrupt change in policy given that he recently stated that policy was accommodative, and the economy did not require such policy anymore. In response, Powell stated ?We think our policy stance is appropriate right now. We do. We also know that our policy rate is now in the range of the committee?s estimates of neutral.? As we discussed in the original article, Powell?s response was incomplete and failed to address the question directly. Given his weak answer, we wonder if Powell knows something we don?t. Could China?s economy be rolling over at a much more concerning pace than anyone thinks? Are trade discussions with China a no-go, therefore resulting in eminent tariffs? Is a bank in trouble?*
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> *The possibilities are endless, but given Powell?s awkward response and unsatisfactory rationale to a simple and obvious question, it is possible that he is hiding something that accounts for the policy U-turn.*

Our Current Take

The market has largely recovered from the fourth quarter swoon, as such the Fed should be resting more comfortably. Economic data remains strong, and if anything it is slightly better than December when the Fed was ready to raise rates three times and put balance sheet reduction on ?autopilot.?

Today the Fed has all but put the kibosh on further rate hikes and, per Mester?s comments, will end balance sheet reduction (QT) in the months ahead.

It is becoming more suspect that the Fed knows something the market does not. What this is, one can only guess. Recent Fed comments are not "measured" nor commensurate with economic data. They fly in the face of their claim that policy will be ?data dependent.?

The stock market may continue to march higher on dovish Fed-speak. **In doing so, it will ignore the elephant in the room, and that is why the Fed is battening down the hatches on such a calm and sunny day.**

When the market discovers the reason for the pivot, volatility may suddenly pick up and the gains resting on the back of a dovish Fed tilt may quickly be erased. Until then enjoy the rally but keep both eyes on the horizon.