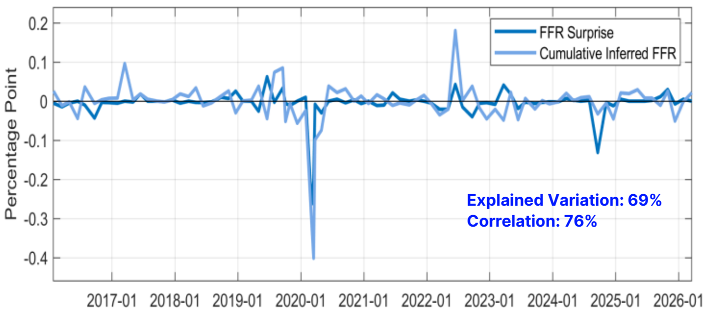
Predictive Power of Inferred Fed Surprises

The Federal Reserve (Fed) policy expectations are a key driver of financial markets, yet traditional measures of policy surprises are only observable around Federal Open Market Committee (FOMC) announcements. This paper introduces "inferred Fed surprises", a novel framework that extends the measurement of Fed policy expectations to all trading days by extracting information from daily movements in Fed funds futures and SOFR futures. The resulting indicators provide a real-time view of how investors revise expectations for future Fed actions as new economic information becomes available.

Exhibit 1: Co-Movement of Fed Funds Rate (FFR) Surprises with Preceding Cumulative Inferred FFR Surprises



Source: State Street Associates, Bloomberg.

Using this framework, we show that changes in the market-implied policy expectations contain valuable information about future asset price movements. In particular, cumulative inferred surprises between FOMC meetings help explain subsequent FOMC-day policy surprises. This finding suggests that while markets often anticipate the direction of future Fed actions, they tend to underestimate the magnitude of the eventual policy surprise. As a result, cumulative inferred surprises can be used to identify situations where market pricing may not fully reflect upcoming policy outcomes, creating opportunities to position in rates and FX markets ahead of FOMC announcements.

The research also demonstrates that inferred policy surprises generated around major macroeconomic releases, such as inflation and employment reports, can identify delayed adjustments in rates and FX markets. Because the implications of economic news for future Fed policy are not always fully reflected immediately, these signals can uncover trading opportunities that persist beyond the initial announcement window.

Together, the findings provide market participants with a practical framework for tracking monetary policy expectations in real time and translating those expectations into actionable investment signals. By connecting daily market repricing to future policy outcomes and asset returns, inferred Fed surprises offer a new lens for understanding, forecasting and trading the impact of Fed policy across rates and FX markets.

For more on this topic, see our 2026 working paper: **"Predictive Power of Inferred Fed Surprises"** by Derin Aksit and Nan R. Zhang.

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