Dissecting the Pre-FOMC Announcement Drift*

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Abstract

Using high-frequency stock level trade data, we study potential drivers of the puzzling upward drift in aggregate equity prices prior to FOMC announcements. We find that purchases dominate as volume falls during the pre-FOMC window. This makes buy trades more informative. The marketwide intraday order imbalance of all size but the smallest can explain the pre-FOMC announcement drift on the market, six size-BM portfolios, and two major ETFs. Market beta completely explains the drift and investor trading behavior in individual stocks. The result is consistent with the hypothesis that institutional investors bet on high beta stocks to beat the market.

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