Fed Watch: This May Be the Last Time

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Key Takeaways

- The Federal Reserve (Fed) kept rates unchanged at the July Federal Open Market Committee (FOMC) meeting, marking the eighth consecutive meeting with no action on the rate front.
- The FOMC is now emphasizing the Fed's dual mandate of inflation and employment, underscoring that risks going forward are now "balanced."
- If upcoming data does continue to "cooperate," it is possible that Chairman Powell could provide forward guidance for a September rate cut at the Kansas City Fed's Jackson Hole Symposium in the second half of August.

Once again, the Fed kept rates unchanged at the July FOMC meeting. As a result, the Fed Funds trading range remains in the 5.25%–5.50% band that was introduced exactly a year ago and still resides at a more than 20-year high watermark. For those keeping track, this represents the eighth consecutive FOMC meeting where the policy maker decided to take no action on the rate front. However, if the inflation and labor market data continue to "cooperate," this may be the last meeting where rates are left unchanged, with expectations for the first rate cut building for the next FOMC gathering in September.

This is exactly where U.S. monetary policy appears to be pivoting. While not explicitly stating that a rate cut is forthcoming at the September FOMC meeting, the voting members seem to be guiding the money and bond markets in that direction. Specifically, the FOMC is highlighting the Fed's dual mandate of inflation and employment rather than solely centering on progress on the price pressure front. Indeed, the emphasis on "balance" when it comes to the risks going forward is the Committee's way of providing forward guidance on the potential for a rate cut.

Another rather important aspect of Fed signaling is Chairman Powell's continued use of the notion of being "confident." In other words, the renewed trend toward disinflation that became evident in the second quarter is providing the springboard for cutting rates without fear of easing policy too soon. By adding the employment aspect back into the equation, the Fed has reintroduced the concept that future decision-making is now data-dependent on not just inflation reports but upcoming labor market data as well.

This is where things could get interesting. At the June FOMC meeting, policy makers dialed back their "dot plot" to show a forecast of only one rate cut rather than the three cuts that were in place beforehand. The release of better-than-expected CPI (and core PCE readings) rendered this "new" dot plot as being almost

immediately obsolete. To be sure, heading into the July policy meeting, implied probabilities for Fed Funds Futures were now showing an expectation of moving toward three rate cuts in 2024.

In fact, once we get that first rate cut out of the way, I continue to emphasize that the central part of the investment landscape going forward will quickly turn to what type of rate-cutting cycle this will look like. If future economic data (think labor markets) does not reveal any signs of visible weakening, then this easing episode will be based on the concept that the current restrictive policy stance is no longer warranted because of the progress on inflation. This backdrop would more than likely result in a more deliberate rate-cutting phase. However, if the Fed were to see higher unemployment rates and continued disinflation in the months ahead, this would arguably create the environment for a more aggressive easing stance.

The Bottom Line

An overarching theme from Powell & Co. in public appearances has been that while rate cuts seem like a reasonable case scenario in the months ahead, Fed officials would still like to see “more data” to get them over that final hurdle. If upcoming data does continue to “cooperate,” it is possible that Chairman Powell could provide such forward guidance at the Kansas City Fed’s Jackson Hole Symposium in the second half of August.