

FOMC meeting, September 17-18

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Meeting minutes: Fed Chair Jerome Powell's growing influence over policy and prescription

The minutes of the September Federal Open Market Committee (FOMC or the Committee) meeting indicated there was a robust discussion around the 50 basis points (bps) fed funds rate cut to 4.75%-5.00%. While a "substantial majority" of participants supported a larger-than-usual rate cut, "some" would have preferred a 25bps cut and a "few others" could have supported a more gradual easing of policy given somewhat elevated inflation, solid economic activity and low unemployment.

The minutes confirmed Fed Chair Powell's significant influence over the FOMC as he managed to convince a majority of his peers that a catch-up rate cut was optimal. Capitalizing on the fact that "almost all" participants saw risks to achieving the Committee's employment and inflation goals as roughly in balance, Powell emphasized the importance of policy recalibration to drive ongoing economic and labor market strength. This forward-looking risk management approach was likely key in convincing most of his colleagues (except Federal Reserve Governor Michelle Bowman, who dissented in favor of a 25bps cut) to depart from a more methodical easing of policy.

Beyond the rate cut decision, policymakers stressed the importance of clear communication. As Powell highlighted during his press conference, the larger rate cut should not be seen as a reaction to a less favorable outlook or a signal that 50bps is the new normal. Fed officials insisted that monetary policy decisions are conditional on the economic outlook and balance of risks, and therefore policy is not on a "preset course."

With regard to the outlook for monetary policy, a "few participants" noted that the overall path of policy normalization, rather than the size of the initial rate cut, would be more important in determining the degree of policy restriction. This notion that the importance of the first rate cut should be minimized is something that we had been stressing since May and was likely a major hurdle preventing the Fed from easing in July.

The tentative Fed pivot away from data-dependency toward a forward-looking perspective has been perceptible in Chair Powell's and New York Fed President John Williams' recent statements. Both noted that if the economy evolves according to the Fed's projections, a 25bps rate cut at each of the two upcoming FOMC meetings would be likely.

Still, given broad-based uncertainty as to the current and expected degree of policy restrictiveness and the level of the neutral rate of interest, most policymakers will likely favor reactionary policy gradualism as their modus operandi.



We anticipate a 25bps rate cut in November but stress that the economic picture will be muddied by recent hurricanes, strikes and Election Day two days before the November FOMC meeting. Unless there is a notable weakening in underlying payroll growth, hours worked and the unemployment rate next month, policy gradualism will likely prevail.

For now, we continue to anticipate the Fed will ease policy by 25bps at every meeting through June of next year. This would translate into 50bps of rate cuts by year-end and another 100bps in H1 2025, putting the fed funds rate at 3.4% in June 2025.

Meeting recap: Fed says, 'Go big, or go home'

The Federal Open Market Committee (FOMC or the Committee) voted to cut the federal funds rate by 50 basis points (bps) to 4.75-5.00%, but the vote saw the first dissent in 19 FOMC meetings with Governor Michele Bowman favoring a 25bps cut. It is likely that a few non-voters favored a more methodical 25bps rate cut since Fed Chairman Jerome Powell noted a "broad" set of officials in favor of the larger cut and that "literally everyone agreed it was time to move ... it's just how big, how fast."

The statement was refurbished to signal balanced risks to the dual mandate, and the dot plot now indicates 100bps of rate cuts this year, up from 25bps in June. While median GDP growth projections were little changed at 2%, inflation projections were revised lower and closer to the 2% target, and the unemployment rate is now seen rising toward 4.4%.

Fed Chair Powell navigated the press conference with agility, pointing to three key takeaways. First, he repeatedly referred to policy "recalibration" to neutralize monetary policy - highlighting the importance of a non-recessionary policy response. The Committee has growing confidence that with appropriate policy recalibration, labor market strength can be maintained. Second, Powell insisted on policy optionality, with the Fed being in a better strategic position to respond to potential risks to the outlook. He stressed the Fed is not on a preset course following what we perceived to be a catchup rate cut. And third, the Fed Chair is now seen to have significant influence over the FOMC as he managed to convince most officials that front-loading cuts was optimal. The bargain is probably that policymakers may be more resistant to rapid easing at the next two policy meetings.

Still, as the Fed embarks on its easing cycle, two old demons continue to haunt it. First, it is essential for policymakers to adopt a robust, forward-looking framework and abandon data (-point) dependency. Unfortunately, that's not the case so far. Powell saying that they might have cut in July if they had had the July jobs report in hand reflects this reactionary stance. Second, policymakers must indicate the destination of travel - the short-term neutral policy rate - and signal how long the journey to a neutralized policy stance is likely to take. This doesn't seem to be part of the Fed's communication strategy.

Unless the labor market weakens significantly, policy gradualism will dominate through year-end - featuring one additional 25bps cut in November and December. Powell noted on multiple occasions that the labor market and the economy are in "solid condition" and that the Fed wants to keep them there. This doesn't show any desire to adopt 50bps cuts as the new normal.

- 1. Easing cycle is underway, with timing and pace in focus:** The FOMC policy statement was altered to signal "risks to achieving the employment and inflation goals are roughly in balance." The economic outlook is uncertain, and the Committee is attentive to the risks to both sides of its dual mandate. A long-overdue removal of the negative conditionality statement for rate cuts allowed for a positive one: "The Committee has gained greater confidence that inflation is moving sustainably toward 2%." Still, the statement didn't go as far as noting that the Committee doesn't "seek or welcome further cooling in labor market conditions."
- 2. On the balance sheet front:** The Fed will continue with a tapered quantitative tightening program with adjusted redemption caps on Treasury securities at \$25b per month and on agency mortgage-backed securities at \$35b.



3. **Dovish dots:** The new interest rate dot plot shifted lower and signaled a more front-loaded easing cycle in response to softening labor conditions.

The median interest rate projection showed an additional 50bps of policy easing expected in 2024 with the fed funds rate at 4.4% in Q4 2024. However, the Committee is almost evenly split on the number of additional rate cuts expected this year, with seven policymakers favoring one additional 25bps rate cut before year-end and nine members favoring 50bps of additional easing, while two policymakers expect no more rate cuts. This signals gradualism through year-end unless economic conditions deteriorate materially. The Q4 2025 median projection was revised lower from 4.1% to 3.3%, indicating another 100bps of rate cuts next year. The estimate of the long-term neutral rate was again revised higher from 2.8% to 2.9% as Fed officials increasingly acknowledge that rates will likely stabilize higher than in the decade pre-pandemic.

4. **Summary of Economic Projections (SEP):** While the growth picture was broadly unchanged, inflation projections were downgraded to reflect continued disinflation in recent months.

The GDP outlook was mostly unchanged with real GDP seen at 2.0% year over year (y/y) in Q4 2024 (versus 2.1% previously) and maintaining that pace of growth through 2027. Meanwhile, the unemployment rate was revised higher to reflect its recent uptrend and is seen rising from 4.2% currently to 4.4% in Q4 2024 (versus 4.0% previously) and Q4 2025 (versus 4.2% previously). In the long run, the unemployment rate is still seen settling at 4.2%.

Fed officials acknowledged the softer inflation data in recent months, with core inflation projections revised markedly lower: personal consumption expenditures (PCE) inflation is seen at 2.3% y/y in Q4, lower than 2.6% in the prior projections. Importantly, core PCE inflation is now expected at 2.6% y/y in Q4 2024 (versus 2.8% previously), while the 2025 projection was slightly downgraded to 2.2% y/y (versus 2.3% previously).

This tells us a couple of things. First, the projections anticipate stronger productivity growth with more growth despite marginally softer employment. Second, the Fed sees the labor market deteriorating further despite a greater degree of policy easing, signaling gradual and partial passthrough of policy onto the economy.

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