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Economics Group

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FOMC Cuts Rates 25 bps, but Two Members Dissent

The committee cut rates 25 bps today, and we look for one more 25 bps rate cut. But two dissents show that the FOMC is not unified in the view that rates need to go significantly lower.

Fed Funds Rate Cut and Balance Sheet Run-off Ends

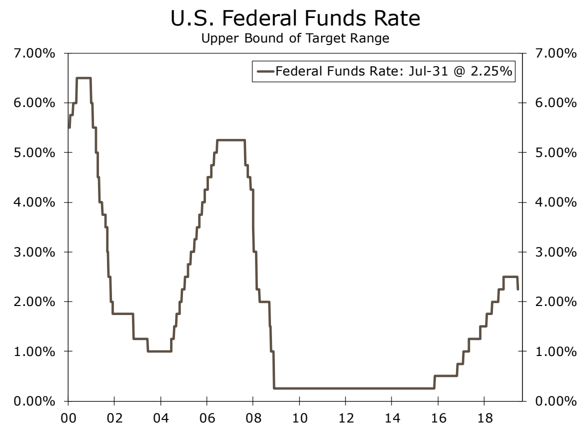
As widely expected, the Federal Open Market Committee (FOMC) decided at its meeting today to reduce the range for the federal funds rate 25 bps. That range now spans 2.00% to 2.25% (top chart). The committee also decided to end the reduction in its balance sheet in August, which has been underway since October 2017. Previously, the FOMC said that it would end its balance sheet run-off in October.

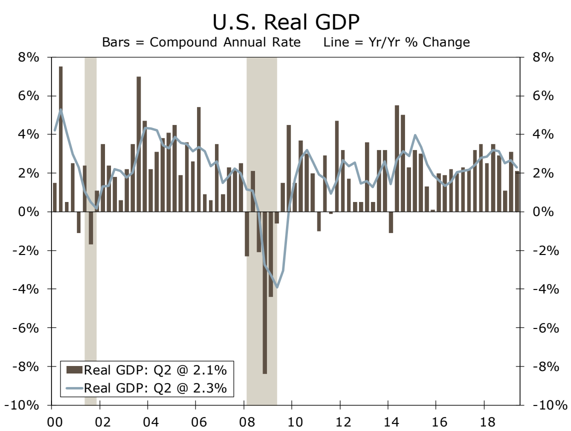
But those two actions were essentially the only nods toward a dovish policy action. For starters, the statement that accompanied today's announcement was very similar to that which was released after the last FOMC meeting on June 19. The committee characterized the labor market as "strong" and said that "economic activity has been rising at a moderate rate" (middle chart). The FOMC went on to say that "growth of household spending has picked up from earlier in the year"—an acknowledgement of the 4.3% annualized growth rate in real personal consumption expenditures in Q2—but that "business fixed investment has been soft." The committee views a sustained expansion in economic activity as the most likely outcome, but acknowledged that there are uncertainties associated with this view.

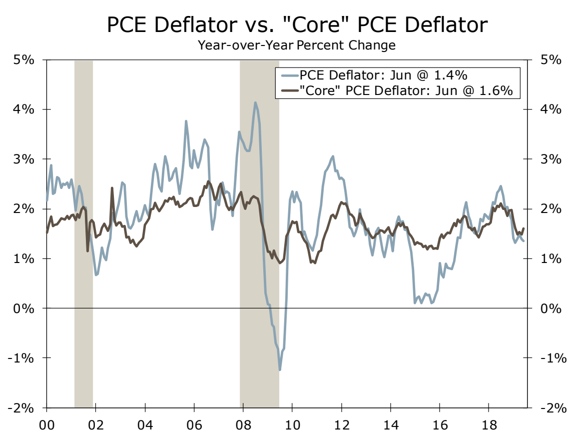
Regarding inflation, the FOMC said that it is "running below 2 percent," which is the Fed's target, and it stated that "market-based measures of inflation compensation remain low" (bottom chart). This undershoot of inflation relative to target and the low level of inflation expectations give the committee room to cut rates further in coming months.

But lower rates in the future are not necessarily preordained. Kansas City Fed President George and Boston Fed President Rosengren dissented from today's rate-cut decision. Both voting members of the FOMC would have preferred to have kept rates on hold, and there may have been additional non-voting members who would have preferred no action as well. (We will get more color on what members thought when the minutes of the meeting are released in a few weeks.) The FOMC is a consensus-driven body, and it will become harder to convince a "critical mass" of committee members to continue easing policy the lower rates go. That said, the FOMC stated that it will be observing a whole range of incoming information as it "contemplates the future path of the fed funds rate."

We continue to look for one additional 25 bps rate cut, probably at the October 30 policy meeting. Today's policy action should be viewed as an "insurance" rate cut. In the context of uncertainties about the economic outlook and below-target inflation, easier policy seems to be warranted. In our view, another 25 bps rate cut would constitute additional "insurance" against a more pronounced slowdown.







Source: Federal Reserve Board, U.S. Department of Commerce and Wells Fargo Securities

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