ECONOMIC UPDATE
REGIONS
October 30, 2019

October FOMC Meeting: Another Cut, Now What?

- The FOMC lowered the Fed funds rate target range by 25 basis points, with the mid-point of the target range now at 1.625 percent
- The Committee in essence adopted a "data dependent" stance, neither implying nor ruling out further funds rate cuts

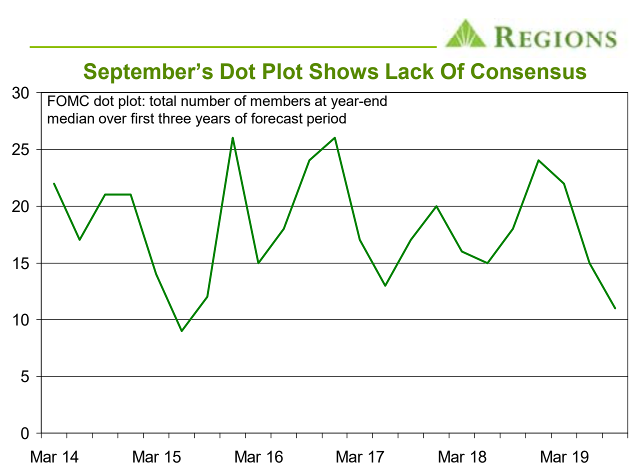
As was widely expected, the FOMC cut the Fed funds rate target range by 25 basis points at the conclusion of their two-day meeting, which puts the mid-point of the target range at 1.625 percent. There was no change in the Committee's assessment of current economic conditions as conveyed in the post-meeting policy statement. There is, however, one significant change in the policy statement, as the Committee removed what had become the familiar pledge to "act as appropriate to sustain the expansion." In today's statement, the Committee states it will continue to monitor the incoming data and assess "the appropriate path of the target range" for the Fed funds rate. As in September, there were two dissents on the vote to lower the Fed funds rate target range, with Boston Fed President Rosengren and Kansas City Fed President George preferring to keep the target range unchanged. It is interesting that St. Louis Fed President Bullard voted in favor of the 25-basis point cut in the funds rate target range after having dissented at the September meeting on the grounds that he favored a 50-basis point cut.

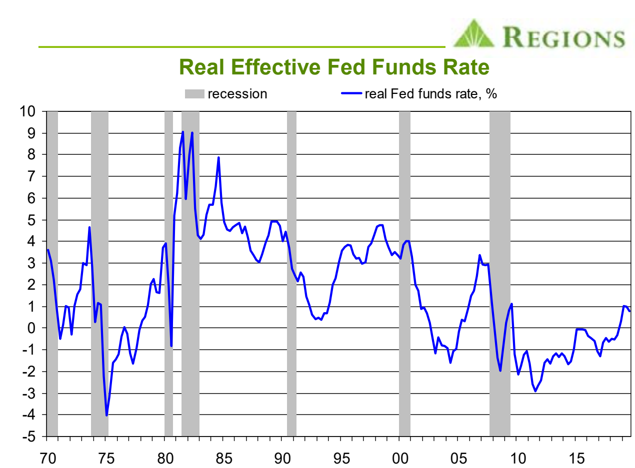
That the Committee's assessment of current economic conditions was left unchanged is, at least to us, a bit surprising. Once again, the Committee notes "economic activity has been rising at a moderate rate." If one is judging solely on the basis real GDP growth, then, sure, repeating this assessment seems warranted. The BEA's initial estimate shows real GDP grew at an annualized rate of 1.9 percent in Q3, little changed from 2.0 percent growth in Q2. Beneath these headlines, however, lie further deterioration in business investment which, if it continues, could at some point weigh on employment as well as acting as a drag on real GDP growth. Additionally, the Committee again states that "job gains have been solid, on average," despite a clear deceleration in the trend rate of job growth. While much of the economic data of late has been on the soft side, suggesting at least some loss of momentum behind economic growth, one gets no sense of this in today's statement.

The change in the forward looking language of the post-meeting policy statement is in essence a roundabout way of the Committee stating that they will be data dependent going forward. Additional funds rate cuts are neither implied nor ruled out, and this more open-ended approach is in line with what market participants had anticipated ahead of this meeting. What was much less certain was how Chairman Powell would message the Committee's stance in his post-meeting press conference.

In his opening comments, Chairman Powell noted that monetary policy is "in a good place," and while the current stance of monetary policy is "likely to remain appropriate" should the economy evolve in line with the Committee's outlook, he also stressed that policy is "not on a pre-set course." When pressed by a questioner as to what it would take to get additional rate cuts, Chairman Powell replied that it would take a "material reassessment of our outlook" and left it at that. In a sense, this is pretty much the only plausible answer Chairman Powell could give if monetary policy is truly not on a pre-set course. In acknowledging weakness in business investment, Chairman Powell noted the risk that this could ultimately spill over into the labor market, but did not seem to attach a very high probability to such an outcome. Even had Chairman Powell expressed more concern over this risk – which we see as a nontrivial risk to the expansion – the question then becomes what the FOMC could be expected to do about it. After all, the price of credit is not the factor holding down business investment, and further rate cuts would do nothing to change the path of business investment. One can infer from Chairman Powell's comments, however, that if the FOMC does see signs of such a transmission, additional rate cuts would follow.

"Material reassessment of our outlook" notwithstanding, there is no clear sense of how high the bar is set for further rate cuts. It is likely that the FOMC itself does not have a clear sense of this. Using entries from the FOMC's "dot plot," our first chart below shows the total number of dots at the year-end medians for the three-year forecast horizon in each set of projections. In the September dot plot, there were only 11 dots at the year-end medians, the fewest since June 2015 and second fewest on record, illustrating the lack of consensus within the Committee. While "data dependent" may be a general guide to the course of monetary policy, that phrase is clearly open to interpretation.





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