

FOMC cuts 25bps for insurance, but are they done yet?

Selena Ling

Head of Strategy & Research

+65 6530 4887

LingSSSelena@ocbc.com

- Fed chair Powell called the Fed's first 25bp rate cut in a decade as a "mid-term policy correction" intended to "insure against downside risks from weak global growth and trade uncertainties".
- Market interpretation is that this is a relatively hawkish easing, hence the profit-taking in Wall Street and front-end of the UST yield curve as players trimmed bets for future rate cuts.
- Tomorrow's nonfarm payrolls, unemployment rate and average hourly earnings data will be key – if the economic data surprises on the strong side, we could see near-term further pressure on the shorter UST bonds.
- We had previously warned that markets would adopt a "buy on rumour and sell on fact" mentality to this Fed easing. Nevertheless, the fact that US-China trade talks have ended inconclusively with only the commitment to keep talking (with the next meeting in early September), US president Trump's sustained pressure ("Powell let us down") on Powell to keep up with monetary policy easing ahead of the 2020 elections and continued signs of global economic momentum deceleration, we keep our call for another 25bps rate cut in September and possibly another 25bps cut in December.

Fed chair Powell called the Fed's first 25bp rate cut in a decade as a "mid-term policy correction" intended to "insure against downside risks from weak global growth and trade uncertainties". However, there were two dissenters, namely Rosengren and George, which coupled with the fact that Powell's positioning this first cut as not opening the door for more cuts to follow, prompted profit-taking on Wall Street and a choppy session for UST bonds. The 10-year yield closed at 2.01% but the front-end of the curve sold off to bear-flatten the yield curve as the futures market trimmed bets for September and December cuts. The Fed also decided to conclude the reduction of its aggregate securities holdings in the System Open Market Account in August, two months earlier than previously indicated.

Fed committee sees a lack of clarity for future interest rate path: The FOMC statement also flagged that "as the Committee contemplates the future path of the target range for the federal funds rate, it will continue to monitor the implications of incoming information for the economic outlook and will act as appropriate to sustain the expansion, with a strong labor market and inflation near its symmetric 2 percent objective". This suggests that there is still significant uncertainty about the interest rate trajectory and future policy moves will be largely dependent. Powell also acknowledged that "at our June meeting, many Committee participants saw

Central Banks

1 August 2019

that the case for lowering the federal funds rate had strengthened, but the Committee wanted to get a better sense of the overall direction of events.”

Baseline economic assessment remains healthy, but reduction in neutral interest rate and unemployment rate. Powell opined that the US economic outlook remains favourable, but noted that muted inflation has already led the Fed to gradually lower its assessment of the policy rate path that would best support that outlook, and that their assessment of the neutral rate of interest and the longer run normal unemployment rate have also declined this year. Powell noted that “we are mindful that inflation’s return to 2 percent may be further delayed, and that continued below-target inflation could lead to a worrisome and difficult-to-reverse downward slide in longer-term expectations”.

We retain our call for another 25bps rate cut in September. While the market interpretation is we’re back to data dependency, the fact that US-China trade talks have ended inconclusively with only the commitment to keep talking (with the next meeting in early September), US president Trump’s sustained pressure on Powell to keep up with monetary policy easing (“Powell let us down”) ahead of the 2020 elections and continued signs of global economic momentum deceleration, we keep our call for another 25bps rate cut in September and possibly still another 25bps cut in December.

Treasury Research & Strategy

Macro Research

Selena Ling*Head of Strategy & Research*LingSSSelena@ocbc.com**Emmanuel Ng***Senior FX Strategist*NqCYEmmanuel@ocbc.com**Tommy Xie Dongming***Head of Greater China Research*XieD@ocbc.com**Terence Wu***FX Strategist*TerenceWu@ocbc.com**Howie Lee***Thailand, Korea & Commodities*HowieLee@ocbc.com**Alan Lau***Malaysia & Indonesia*AlanLau@ocbc.com**Carie Li***Hong Kong & Macau*carierli@ocbcwh.com**Dick Yu***Hong Kong & Macau*treasuryresearch@ocbc.com

Credit Research

Andrew Wong*Credit Research Analyst*WongVKAM@ocbc.com**Ezien Hoo***Credit Research Analyst*EzienHoo@ocbc.com**Wong Hong Wei***Credit Research Analyst*WongHongWei@ocbc.com**Seow Zhi Qi***Credit Research Analyst*ZhiQiSeow@ocbc.com

This publication is solely for information purposes only and may not be published, circulated, reproduced or distributed in whole or in part to any other person without our prior written consent. This publication should not be construed as an offer or solicitation for the subscription, purchase or sale of the securities/instruments mentioned herein. Any forecast on the economy, stock market, bond market and economic trends of the markets provided is not necessarily indicative of the future or likely performance of the securities/instruments. Whilst the information contained herein has been compiled from sources believed to be reliable and we have taken all reasonable care to ensure that the information contained in this publication is not untrue or misleading at the time of publication, we cannot guarantee and we make no representation as to its accuracy or completeness, and you should not act on it without first independently verifying its contents. The securities/instruments mentioned in this publication may not be suitable for investment by all investors. Any opinion or estimate contained in this report is subject to change without notice. We have not given any consideration to and we have not made any investigation of the investment objectives, financial situation or particular needs of the recipient or any class of persons, and accordingly, no warranty whatsoever is given and no liability whatsoever is accepted for any loss arising whether directly or indirectly as a result of the recipient or any class of persons acting on such information or opinion or estimate. This publication may cover a wide range of topics and is not intended to be a comprehensive study or to provide any recommendation or advice on personal investing or financial planning. Accordingly, they should not be relied on or treated as a substitute for specific advice concerning individual situations. Please seek advice from a financial adviser regarding the suitability of any investment product taking into account your specific investment objectives, financial situation or particular needs before you make a commitment to purchase the investment product. OCBC Bank, its related companies, their respective directors and/or employees (collectively "Related Persons") may or might have in the future interests in the investment products or the issuers mentioned herein. Such interests include effecting transactions in such investment products, and providing broking, investment banking and other financial services to such issuers. OCBC Bank and its Related Persons may also be related to, and receive fees from, providers of such investment products.

This report is intended for your sole use and information. By accepting this report, you agree that you shall not share, communicate, distribute, deliver a copy of or otherwise disclose in any way all or any part of this report or any information contained herein (such report, part thereof and information, "Relevant Materials") to any person or entity (including, without limitation, any overseas office, affiliate, parent entity, subsidiary entity or related entity) (any such person or entity, a "Relevant Entity") in breach of any law, rule, regulation, guidance or similar. In particular, you agree not to share, communicate, distribute, deliver or otherwise disclose any Relevant Materials to any Relevant Entity that is subject to the Markets in Financial Instruments Directive (2014/65/EU) ("MiFID") and the EU's Markets in Financial Instruments Regulation (600/2014) ("MiFIR") (together referred to as "MiFID II"), or any part thereof, as implemented in any jurisdiction. No member of the OCBC Group shall be liable or responsible for the compliance by you or any Relevant Entity with any law, rule, regulation, guidance or similar (including, without limitation, MiFID II, as implemented in any jurisdiction).