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 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
NgCYEmmanuel@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

Co.Reg.no.:193200032W