First Trust
ECONOMIC RESEARCH REPORT
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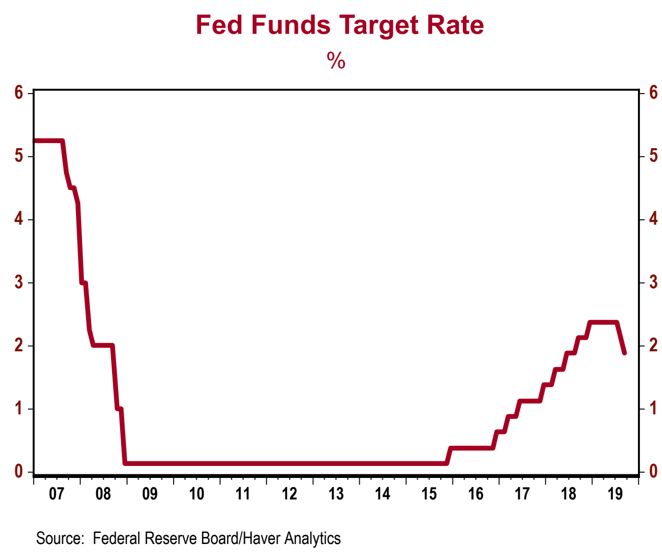
September 18, 2019 • 630.517.7756 • www.ftportfolios.com

It's Not You, It's Me

As expected, the Fed cut short-term interest rates by 25 basis points today, moving the range for the federal funds rate down to 1.75 - 2.00%. At the same time, it lowered the interest rate on excess reserves (IOER) to 1.8% and the re-purchase (repo) rate to 1.7%, five basis points below the bottom of the Fed Funds range. In his press conference, Chair Powell confirmed these were "technical changes" in reaction to repo rate pressures earlier this week. We published a piece earlier today with our thoughts in the repo market jitters, but suffice it to say we see the issues coming from poor regulatory policy, not a lack of money in the system.



Oddly, while cutting rates, the Fed made only minor changes to its economic outlook, doubling-down on the move away from data dependence. Perhaps that's why there are now more quarrels within the Fed itself, with three voting members dissenting. Kansas City Fed President Esther George and Boston Fed President Eric Rosengren voted today to keep rates unchanged, while St. Louis Fed President James Bullard voted to cut rates by 50 basis points.

Chair Powell highlighted two reasons for moving rates. First, business "uncertainty" and slower global growth - which seem to have passed employment and inflation as areas of focus for the Fed, despite admission by the Fed that it doesn't have the tools to impact the trade dispute - have the Fed concerned about future growth. And second, Powell stated that the Fed's view on the appropriate level of rates to sustain growth have "changed significantly" towards a lower path. If the data doesn't support your actions, move the goal post. It's the policy justification equivalent of saying "It's not you, it's me."

All that said, the dot plot suggests no more rate cuts in 2019. But take that with a grain of salt. No further rate cuts are needed in our view (on a nominal basis the U.S. economy has grown at a 5% annualized rate over the past eight quarters), and we don't think either of this year's rate cuts were justified, but the Fed seems tilted towards action. In Fed forecasts as recently as June, the median dot in the dot plot showed no rate cuts this year. Since then the Fed has cut rates twice. Our best guess is that the Fed will probably – not definitely, but probably – cut rates one more time in 2019, and, if so, more likely reduce rates in December than October.

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Text of the Federal Reserve's Statement:

Information received since the Federal Open Market Committee met in July indicates that the labor market remains strong and that economic activity has been rising at a moderate rate. Job gains have been solid, on average, in recent months, and the unemployment rate has remained low. Although household spending has been rising at a strong pace, business fixed investment and exports have weakened. On a 12-month basis, overall inflation and inflation for items other than food and energy are running below 2 percent. Market-based measures of inflation compensation remain low; survey-based measures of longer-term inflation expectations are little changed.

Consistent with its statutory mandate, the Committee seeks to foster maximum employment and price stability. In light of the implications of global developments for the economic outlook as well as muted inflation pressures, the Committee decided to lower the target range for the federal funds rate to 1-3/4 to 2 percent. This action supports the Committee's view that sustained expansion of economic activity, strong labor market conditions, and inflation near the Committee's symmetric 2 percent objective are the most likely outcomes, but uncertainties about this outlook remain. 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.

In determining the timing and size of future adjustments to the target range for the federal funds rate, the Committee will assess realized and expected economic conditions relative to its maximum employment objective and its symmetric 2 percent inflation objective. This assessment will take into *account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments.*

Voting for the monetary policy action were Jerome H. Powell, Chair, John C. Williams, Vice Chair; Michelle W. Bowman; Lael Brainard; Richard H. Clarida; Charles L. Evans; and Randal K. Quarles. Voting against the action were James Bullard, who preferred at this meeting to lower the target range for the federal funds rate to 1-1/2 to 1-3/4 percent; and Esther L. George and Eric S. Rosengren, who preferred to maintain the target range at 2 percent to 2-1/4 percent.