Market Insights

Fed Cuts Rates by 0.25% at October Meeting

LIQUIDITY | GLOBAL LIQUIDITY TEAM | MARKET INSIGHT | October 30, 2019

The Federal Open Market Committee (FOMC) lowered the range for the federal funds rate by 0.25% to 1.50%-1.75% during its October meeting. Chair Jerome Powell highlighted that global developments and muted inflation were the main drivers behind the policy decision. Powell noted its current monetary policy stance is likely to remain appropriate as long as there is no material reassessment to the Fed's economic outlook.

FOMC Meeting Summary[1]

- **Monetary Policy Decisions**
  - The FOMC voted to lower the target range for the Fed funds rate by 0.25% to 1.50%-1.75%
  - Lowered the interest on excess reserves (IOER) by 0.25% to 1.55% from 1.80%
  - The Fed will "continue to monitor the implications of incoming information for the economic outlook as it assesses the appropriate path," removing "will act as appropriate to sustain the expansion" from prior statements
  - Two FOMC members, Esther George and Eric Rosengren, dissented to the decision arguing to keep the target range unchanged at 1.75%-2.00%

- **Economic Conditions**
  - Chairman Powell acknowledged that job growth has slowed but remains solid while the unemployment rate has remained low
  - Powell also noted that household spending has risen at a strong pace
  - Business fixed investment and exports "remain weak" in addition to declining manufacturing output
  - The FOMC stated both headline and core inflation are running below 2%

- **Policy Outlook**
  - The Fed will remain data dependent while it "assesses the appropriate path" for monetary policy
  - Powell noted the current federal funds target rate is likely to remain appropriate as long as there is no material reassessment to the Fed's economic outlook, which is moderate economic growth, strong labor market, and inflation moving closer to its 2% target
  - The baseline outcome for an economy in the eleventh year of an expansion is "favorable"
  - Chairman Powell views a phase one trade deal between the U.S. and China as a positive outcome for the global economy

[1] Source: FOMC October 30, 2019 Statement.

- **Portfolio Strategy**
  - **Prime Strategies** - Leading up to the October FOMC meeting, where a 25 basis point interest rate cut was widely expected by the market, both one-month and three-month London Interbank Offered Rate (Libor) declined throughout the month, setting at 1.78 and 1.91 percent respectively as of October 30. As yields moved lower, we opportunistically added duration to the portfolios, purchasing fixed rate and quarterly resetting floating rate securities in the six and nine month tenors. With Fed Chair Powell dropping their pledge to “act as appropriate” in favor of “monitoring the implications of incoming information,” we continue to manage our portfolios from a conservative positioning standpoint, maintaining our emphasis on high levels of weekly liquidity and structuring our portfolios to respond to changes in monetary policy.
  - **Government Strategies** - The yield curve continued to flatten as demand for treasuries was very strong in October. The Fed announced and began its plan to increase bank reserves by purchasing $60 billion in treasury bills through at least the start of the second quarter, which certainly contributed to bill demand. We bought both fixed-rate agencies and treasuries maturing within one- to six- month tenors and floating-rate securities in various maturities. The FOMC acted as expected with a 25 basis point cut this month. The removal of “act as appropriate” from its policy statement implies that additional rate easing is less likely for the rest of this year. We continue to ensure high levels of liquidity and manage the portfolios to be responsive to changes in market conditions and interest rate levels.

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