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TD Economics

Commentary

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FOMC CUTS THE FED FUNDS RATE BY 25BPS AND LEAVES NEUTRAL BIAS

- **The FOMC cut the fed funds rate by 25bps to 2%. Discount rate was cut by 25bps also, to 2.25%**
- **The vote was 8-2, with dissent from Fed Presidents Fisher and Plosser.**
- **The statement highlighted ongoing weakness in the economy but left out any mention of forward looking action.**

As widely expected the FOMC cut the fed funds rate by 25bps to 2% today. The vote was close but there were two dissenters similar to the last meeting. They were Dallas Fed President Fisher and Philadelphia Fed President Plosser, both noted inflation hawks who dissented at the March 18 meeting.

Given that the rate cut was largely priced in, the focus was really on what the Fed said in the statement. The economic assessment was not quite as bad as feared. There is still a good deal of softness in the U.S. economy with household and business spending remaining "subdued." In addition, labour markets "have softened further." Moreover, the Fed mentioned that "financial markets remain under considerable stress," which comes as little surprise. The housing contraction is also presumed to remain a drag on growth going forward.

On the inflation front, there was a small surprise in that the Fed noted that "readings on core inflation have improved somewhat." However, they acknowledge that "energy and other commodity prices have increased and some indicators of inflation expectations have risen in recent months." Recent price trends in energy and food have probably been fodder for the two inflation hawks, like Plosser and Fisher, and were clearly bolstering their view for dissent.

With respect to the bias, the Fed was uncharacteristically mum about the matter. The interpretation of this statement suggests that the hawks may be growing in fortitude, in that they do not make any mention of downside risk. Moreover, their lack of explicit bias suggests that the Fed is neither signalling another rate cut going forward, but by not mentioning a bias, they are leaving the door open for another cut, should it become necessary.

Looking ahead, we continue to expect the Fed to deliver an additional 75bps of rate cuts, based upon our below consensus economic view. The way the Fed details the weakness in the economy suggests scope for a bit more monetary stimulus, but there is clearly a need to see how the balance of risks between growth and inflation unfold.

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