Deutsche Bank
Chief Investment Office

CIO Memo

September 18, 2024

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FOMC: A September to remember

Key takeaways

- The Federal Open Market Committee (FOMC) delivered its first 50bps rate cut bringing down the rate to 4.75% - 5.00%.
- Alongside the expected decision to cut rates, the FOMC also updated its Summary of Economic Projections (SEP), indicating 100bps of cuts to 4.4% by the end of the year.
- Although investors initially reacted positively to the significant rate cut, equity markets closed negatively as it raised concerns that the economy had cooled more than expected.

1. What happened?

The FOMC announced its decision to lower the Fed Funds Rate by 50bps to 4.75% - 5.00%. The decision to cut rates this month was accompanied by an FOMC statement that included notable updates from the previous meeting. The FOMC acknowledged that job gains had “slowed” and while inflation still remains “somewhat elevated”, the committee has gained the much needed “confidence” that the inflation is moving toward the ideal 2% target.

Along with the decision to cut rates, the FOMC also released its latest Summary of Economic Projections (SEP). The projections showed the median rate moving down to 4.4% for 2024, implying that the Federal Reserve now expects two additional 25-basis point rate cuts this year.

The dispersion in the latest ‘dot plot’ rate projections from the respective FOMC members was mostly on-par with the prior SEP signaling better consensus amongst the members. When assessing the estimates for rate cuts this year, the new central tendency expectations for 2024 and 2025 lie between 4.4-4.6 and 3.1-3.6, lower than the 4.9-5.4 and 3.9-4.4 respectively expected in the last release.

Revisions were also seen in some of the FOMC’s economic forecasts. The GDP growth rate for 2024 was revised down from 2.1% to 2.0%. The unemployment rate was revised up from 4.0% to 4.4%. Regarding inflation, PCE expectations were revised down to 2.3% from 2.6% and core PCE was revised down from 2.8% to 2.6%, indicating that FOMC expects inflation to continue in its disinflationary track.

During the press conference, Chairman Jerome Powell noted that the economy remains strong overall and has cooled from its ‘overheated state’. He reiterated the Fed’s commitment to the dual mandate of achieving maximum employment while upholding price stability and that the restrictive monetary policy has helped strike a “balance” between aggregate supply and demand. Chairman Powell highlighted that the Fed will continue to make decisions meeting by meeting and this 50bps rate cut does not necessarily set a “new pace” or precedent for future rate cuts.

2. How did markets react?

Overall, markets reacted negatively to the release of the FOMC statement and subsequent ‘dot-plot’ updates. At the time of writing, both the S&P 500 and NASDAQ were trading in negative territory, reaching -0.29% and -0.31% respectively. Both the 2-Year and 10-Year Treasury yields increased to 3.60% and 3.69% respectively.

3. What does it mean for investors?

Today’s FOMC meeting saw the Fed deliver its first rate cut in four years. While base expectations were more in line for a 25bps rate cut, the 50bps rate cut signaled the economy has reacted more than appropriately to the Fed’s longstanding tight monetary policy. With unemployment rates currently at 4.2% (with a forecasted peak rate of 4.4%) and inflation at 2.5%, continuing on its disinflationary track, the Fed has delivered a ‘timely’ rate cut to better balance out the economy.

Although the median expectation is for two further 25bps rate cuts before the end of 2024, there is dispersion amongst the FOMC participants highlighting a slight uncertainty in the future path of inflation - 1 member expects three rate cuts, 9 members expect two rate cuts, 8 members expect one rate cut and 2 members expect for no cuts at all for the remainder of the year. With the new FOMC statement stating that inflations still remains ‘somewhat elevated’, it was no surprise that the longer-term estimates of the Federal Funds Rate showed an increase from 2.8% to 2.9%.

In his remarks, Chairman Powell had noted that while inflation is moving closer to objective with ‘diminished’ upside risks to inflation, there is an increased downside risk to employment given the cooling labor market. The FOMC will be attentive to risks on both sides of the dual mandate as it aims to navigate the economy towards a ‘neutral’. Given the Fed’s data dependent stance, they will continue to monitor upcoming labor market, inflation and other data points to determine the trajectory of rate cuts for the rest of 2024.

Today’s significant, but not unexpected, 50bps rate cut will pave a way for lower borrowing costs for consumers and businesses alike. However, the future trajectory of rate cuts is not conclusive as the Fed very much depends on upcoming data points to effectively recalibrate the economy towards the ideal 2% inflation goal.

Glossary

The Fed funds rate is the interest rate at which depository institutions lend overnight to other depository institutions.

The Federal Reserve (Fed) is the central bank of the United States. Its Federal Open Market Committee (FOMC) meets to determine interest rate policy.

'Mark-to-Market' typically describes an accounting practice that involves adjusting the value of an asset to reflect its value as determined by current market conditions.

Four times a year, the Federal Reserve releases a Summary of Economic Projections (SEP) for GDP growth, the unemployment rate, inflation, and the appropriate policy interest rates.

The FOMC Dot Plot is comprised typically of 19 dots: seven members of the Board of Governors of the Federal Reserve System and presidents of the 12 regional banks. Each is asked to indicate where they believe the Federal Funds rate should be in the future.

The Personal Consumption Expenditure (PCE) is a price index for goods and services, particularly relevant to the context of U.S. GDP

Treasuries are bonds issued by the U.S. government.

USD is the currency code for the U.S. Dollar.

Historical Performance

Performance	9.18.2019 - 9.18.2020	9.18.2020 - 9.18.2021	9.18.2021 - 9.18.2022	9.18.2022 - 9.18.2023	9.18.2023 - 9.18.2024
S&P 500	12.5%	35.5%	-11.3%	16.9%	28.4%
NASDAQ	32.0%	39.4%	-23.9%	19.8%	28.2%
2-Year U.S. Treasury	3.9%	0.1%	-3.3%	0.8%	4.5%
10-Year U.S. Treasury	13.7%	-5.6%	-10.3%	-4.8%	-0.1%

Source: LSEG Datastream, Deutsche Bank AG. Data as of September 18th , 2024.

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