

The Fed cuts by 25bp, and hints at more gradual cuts in the future

The US Fed has cut its policy rate by 25bp. They acknowledge that policy remains restrictive and that further cuts are likely but that the pace of those cuts may slow. They were reluctant to discuss the 'Trump effect', but here's the risk: slightly firmer growth with more inflationary pressures. And that might lead to a less aggressive rate-cut narrative



Fed Chair, Jerome Powell, in Washington last month

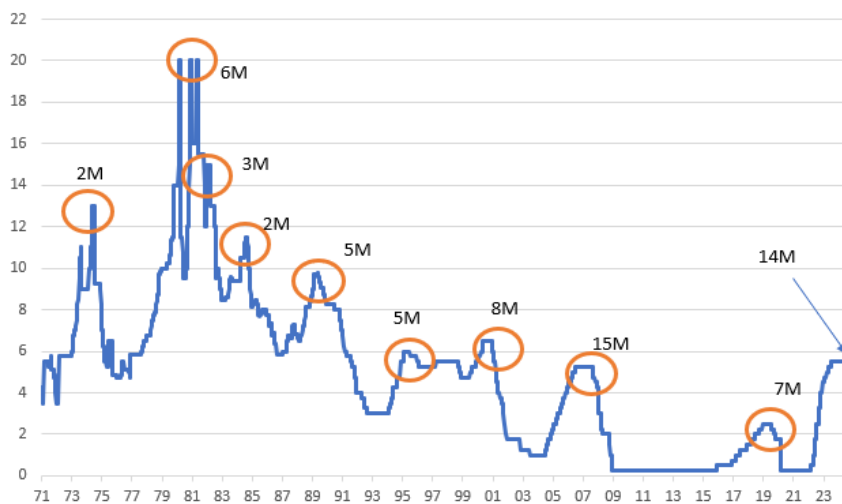
25bp cut but policy remains "restrictive"

As almost universally expected, the Federal Reserve has cut rates by 25bp to leave the target range for the federal funds rate at 4.5-4.75%. It was a unanimous decision this time (Michelle Bowman voted for 25bp rather than the 50bp cut the Fed delivered in September), and there were only minor tweaks in the statement. There was a bit of market excitement initially when it was spotted that the Fed said *inflation has made progress toward* 2% rather than *further progress* as written in September, but this was a very minor shift.

It also appeared that Chair Powell wanted to give as little away as possible on the implications of a Trump Presidency. Powell refused to 'speculate' on what it may mean at the press conference,

with fiscal policy only going into their models once it is enacted. Nonetheless, he did state that monetary policy remains 'restrictive' and they will continue to decide policy on a meeting-by-meeting basis although, as they get closer to neutral, it may be 'appropriate' to slow the pace of interest rate cuts.

Fed funds ceiling rate with duration between last hike in a cycle and first rate cut



Source: Macrobond, ING

A more gradual rate cut profile looks likely

In terms of where we go from here, inflation is looking better behaved and the jobs market is cooling but not collapsing, so the Fed is in a position to continue loosening monetary policy closer to neutral gradually. We think they will cut by 25bp again in December, but the outlook thereafter is less clear and there is a strong chance of a pause at the January FOMC meeting.

Previously, the market was expecting the Fed funds rate to bottom somewhere in the 3-3.5% area by next summer. With Donald Trump winning the presidency, his key policy thrusts are extended and expanded, including tax cuts, tariffs, and immigration controls. This may keep the growth story more supported in the near term, but there is likely to be more concern at the Fed about the inflation implications from trade protectionism and labour supply constraints. As such, the market has moved to price a slower, more gradual easing cycle with a slightly higher terminal rate of 3.5-3.75%. We agree with this right now.

Nonetheless, the cooling jobs market remains an important story, while the sharp move higher in longer-dated Treasury yields (80-90bp higher since the Fed cut rates in September) could become a significant headwind for growth. We now forecast the 10Y yield could rise above 5% in 2025 on fiscal sustainability and inflation worries. This will push consumer and corporate borrowing costs and could become a major headwind for growth.

Fed will soon tell us what they think Trump 2.0 means

Like the rest of us, the Fed only has an early sense of the direction of travel post-election; what Trump proposed during his campaign and what he eventually delivers as president may be very

different. The Fed won't want to pre-empt a set of policies that may not come to fruition. However, they will be releasing new economic projections at the December FOMC meetings, and their call on what Trump 2.0 might mean will be fascinating.

Our view is that while the growth trajectory in the near term a little more encouraging, the more aggressive he goes on trade and immigration policies and the higher Treasury yields push, the more challenges this may present for the US economy over time.

Dollar and Treasuries dominated by retracement activity

The FOMC meeting and press conference have not had much of an impact on the FX and debt markets. If there was any move during the press conference, it was briefly to a slightly firmer dollar and a 5bp rise in short-dated US Treasury yields when Chair Powell seemed to imply that downside economic risks had receded compared to when the Fed was putting together its economic projections in September.

One interesting question was whether the 75bp climb in US Treasury 10-year yields had tightened financial conditions enough to be material to the Fed. Powell didn't think so and blamed the rise in yields on better growth prospects rather than on inflation.

However, today's widely expected rate cut and neutral press conference took a back seat to retracement activity in the FX and Treasury markets. Today, the dollar and US 10 yields have roughly retraced half of their election-day surge. Driving today's trade is likely position adjustment after a near one-way run in both markets since early October.

We cannot rule out some modest further retracement here as investors continue to pocket any gains after a steady six-week trend. Yet, the prospects of looser fiscal and less dovish Fed policy through 2025 should limit the downside to both the dollar and especially long-dated US Treasury yields over the coming weeks and months. Please see the latest [ING Monthly](#) for more on our FX and Rate views.

Author

James Knightley

Chief International Economist, US

james.knightley@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s),

as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.