

No Rate Cut Yet, but the Clouds Are Parting

Fed officials again kept the federal funds rate at 5.25–5.50%. We believe they'll cut for the first time this cycle in September and then analyze incoming data to inform future rate-cut decisions.

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Topic

Market Events

Key takeaways

- We believe the Fed will cut rates for the first time this cycle at its September meeting as long as incoming data continue to align with our expectations.
- Progress on inflation accelerated over the past few months. Unemployment, however, ticked up to 4.1% in June. A weakening labor market could be the key challenge for the economy going forward.
- We continue to favor bonds, which benefit from moderating growth and moderating inflation. We also continue to like equities and expect broadening of the equity rally ahead.

As expected, the Federal Open Market Committee decided to keep its key interest rate, the federal funds rate, unchanged at 5.25–5.50%. We believe the Federal Reserve (Fed) will cut rates for the first time this cycle at its September meeting as long as incoming data continue to align with our expectations.

Progress on inflation accelerated over the past few months across a broad range of measures. The [Personal Consumption Expenditures Price Index \(PCE\)](#)—the Fed's preferred measure of prices—declined to 2.5% in June, continuing a pattern since April of coming in below consensus expectations. While core PCE (which excludes food and fuel) is slightly elevated, we believe enough progress has been made given the growth backdrop. Breadth—the number of goods and services in a basket that represents typical consumer spending whose prices are rising versus falling—continues to decline. U.S. growth ticked slightly higher in the second quarter of 2024, to 2.8% compared with 1.4% in the first quarter, but the overall growth picture remains reasonable.

We're monitoring key labor market data. U3 unemployment, which is the total unemployed as a percent of the U.S. civilian labor force, ticked up to 4.1% in June. Soft data (data that generally involve opinions, attitudes, and/or feelings) support a weakening labor market as the key challenge for the economy going forward. Services employment data have continued to deteriorate.

Our base case is for the Fed to make its first cut in September and remain neutral from a forward guidance perspective, analyzing incoming data to inform future rate-cut decisions. Growth and jobs are not yet at a point that justifies a prolonged cutting cycle and less-restrictive monetary policy. We expect to see conditions deteriorate and thereby support further rate cuts later in the fourth quarter of 2024.

We continue to favor bonds, which benefit from moderating growth and moderating inflation, particularly internationally. We also continue to like equities. We expect broadening of the

equity rally, and any relief from perceived looser monetary policy would likely support equity prices in the medium term.

Geopolitical uncertainty in the U.S. has increased in July, and we expect the Fed will take this situation into account in its decision-making.

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