Daiwa Capital Markets

U.S. Data Review

- FOMC: divided views, but look for continued support

Michael Moran
Daiwa Capital Markets America
212-612-6392
michael.moran@us.daiwacm.com

Minutes from the July FOMC Meeting

Our main take-away from the minutes of the July meeting of the Federal Open Market Committee was that officials held widely divergent views on the proper course for monetary policy. While the Committee adopted a 25 basis point cut in the federal funds rate, a “couple” of meeting participants (voters and non-voters combined) preferred to trim rates by 50 basis points. At the other extreme, “several” officials wanted to hold policy steady, and two officials in this group dissented from the decision to cut interest rates (Ester George of the Kansas City Fed and Eric Rosengren of the Boston Fed).

The minutes attempted to present a strong case for Fed easing, highlighting in bullet format -- an unusual configuration for the minutes -- three reasons for cutting interest rates. In summary:

- Signs of slower growth had emerged in the U.S. (business investment, manufacturing) and many foreign economies had softened, especially China and several in Europe
- Downside risks to the economic outlook remained in place, especially risks associated with foreign economic activity and international trade
- Inflation remained subdued, and wage pressure remained moderate despite a low unemployment rate

Although the minutes outlined a clear explanation for Fed easing, the meeting summary also suggested considerable variation in views and lack of a strong consensus on how to proceed. While officials were aware of some soft spots in the economy, most seemed to view the economy’s performance and its outlook as favorable. The committee recognized downside risks, but officials “generally judged that downside risks to the outlook for economic activity had diminished somewhat since their June meeting.” Inflation was subdued, but “many” participants noted that transitory factors had restrained inflation and that the trimmed mean PCE price index was “running around 2 percent.”

The minutes contained only one short (and vague) paragraph on how the Committee might proceed in the months ahead. Officials planned to be guided by incoming information and they hoped to avoid the appearance of following a pre-set course. Officials emphasized the importance of remaining flexible. This paragraph also mentioned the characterization of the policy change introduced by Chair Powell at his press conference: officials viewed it as “a mid-cycle adjustment.”

While the minutes did not offer much guidance on upcoming changes, we viewed one passage as suggesting that officials will adopt at least one additional cut. The minutes noted an improvement in financial conditions since the previous FOMC meeting, but that improvement seemed to be based on the view that the Fed would be easing. While the economic data and perceived risks did not provide a clear-cut case for a rate cut, officials seemed to realize that failure to validate market expectations would cause market disruption. Investors and traders are looking for additional support from the Fed, and we doubt that policymakers will frustrate those expectations.