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Review: FOMC Cuts Rates by 25bps,

And Foresees Further Easing Ahead

by

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Executive Summary

- **Decision Made**: *The Fed cut US interest rates in September.* The FOMC its target Fed funds range by 25 bps to 4.00% - 4.25%. The Fed maintained its data-dependent approach, signalling that rate decisions will continue to be made on a meeting-by-meeting basis. Officials signaled two more cuts this year amid rising labor market risks. The decision drew dissent from the newly appointed Stephen Miran, who wanted a larger 50bps cut at this meeting.
- **Policy Discussion**: *Powell framed the 25bp cut as a "risk management" step to safeguard the economy, not a response to an active downturn*. The Fed signaled two more cuts this year, though the dot plot showed wide divergence—one projection, likely from new Governor Miran, called for 125bps of easing. Beyond 2025, officials penciled in just one cut in 2026 and another in 2027, moving rates closer to the 3% neutral level. Most of Trump's appointees backed the move, with Miran dissenting in favor of a larger 50bp cut. Powell stressed that outsized moves are reserved for times when policy is clearly misaligned, suggesting no urgency for such action now.

  The discussion highlighted shifting priorities, with less concern over tariff-driven inflation and greater focus on slowing growth and rising unemployment. Powell noted both labor supply and demand have weakened, with job creation now below the breakeven rate needed to stabilize unemployment. While tariffs are raising goods prices, the Fed views the effect as temporary, attributing labor weakness more to reduced immigration and softer labor force growth. Powell also reaffirmed the Fed's independence, underscoring that decisions are data-driven and long-term in focus. He avoided comment on Treasury Secretary Bessent's call for an independent review, his own term ending in May, or Trump's push to remove Governor Lisa Cook, framing them as political or legal issues outside the Fed's remit.
- **Changes To Economic Forecasts:** *The Fed projects the funds rate at 3.6% by year-end, down from 3.9% in June, signaling a new easing cycle after last year's 100bp cuts.* One more cut is expected in 2026, with rates seen at 3.4% in 2026 and 3.1% in 2027. The rates outlook was shifted 25bps lower compared to June. Views remain split, with most officials favoring at least one cut this year and one projecting six. The SEP shows core inflation at 3.1% this year, easing to 2.6% in 2026 and 2.1% in 2027, while unemployment is forecast to rise to 4.5% this year before edging lower. GDP growth was revised up to 1.6% in 2025 and 1.9% in 2027. Risks remain tilted upward for inflation and downward for jobs, prompting a shift toward a more neutral stance.

Key Picture: US Federal Reserve Forecasts – 2025-2027

	2025*f*			2026*f*		2027*f*		2028*f*	Longer Run	
	Latest Reading	September Report	June Report	September Report	June Report	September Report	June Report	September Report	September Report	June Report
GDP *(real growth, y-o-y)*	2.0	1.6	1.4	1.8	1.6	1.9	1.8	1.8	1.8	1.8
Unemployment rate *(%, y-o-y)*	4.3	4.5	4.5	4.4	4.5	4.3	4.4	4.2	4.2	4.2
PCE Inflation *(%, y-o-y)*	2.6	3.0	3.0	2.6	2.4	2.1	2.1	2.0	2.0	2.0
Core PCE Inflat. *(%, y-o-y)*	2.9	3.1	3.1	2.6	2.4	2.1	2.1	2.0	-	-
Federal Funds Rate *(%)*	4.327	3.6	3.9	3.4	3.6	3.1	3.4	3.1	3.0	3.0

Source: Federal Reserve '*Summary of Economic Projections*' June and September 2025. *Note:* 1. GDP reading for Q1-2025; 2. Unemployment rate as of August 2025; 3. PCE and core PCE inflation as of July 2025; 4. Projections reflect the median of FOMC projections

Analysis

- **DECISION MADE**: *On September 17, the US Federal Reserve's FOMC cut its Fed funds range by 25 bps to 4.00% - 4.25%.* FOMC was divided: Powell and 10 others voted for the policy; Miran opposed, favoring a rate cut of 50 bps. At the July meeting, Governors Michelle Bowman and Christopher Waller pushed for a 25bp cut but accepted the reduction approved in September. All three governors, appointed by Trump, face pressure from him to accelerate rate cuts.

  Regarding *forward guidance*, the Fed continues to be data-dependent with decisions being made meeting by meeting. In its updated statement, the Fed noted a modest rise in unemployment and a "shift" in risk balance. The FOMC's statement adjusted its assessment of economic conditions. The committee again described economic activity as "moderated," while adding that "job gains have slowed" and inflation "has moved up and remains somewhat elevated." Weaker job growth alongside higher inflation underscores the tension between the Fed's dual goals of stable prices and maximum employment. The statement also states that uncertainty "remains elevated," a more cautious view than in June, when the committee noted it had "diminished but remains elevated."

  Regarding *balance sheet policies*, the Fed in May last year decided to slow down the pace of QT from June. The Committee plans to further decrease its Treasury securities, agency debt, and agency mortgage-backed securities holdings. Starting in April, the Committee slowed the reduction of its securities holdings by lowering the monthly Treasury redemption cap from $25 billion to $5 billion, while keeping the agency debt and mortgage-backed securities cap at $35 billion.

- **POLICY DISCUSSION:** *Powell characterized the rate cut as a "risk management" step, aimed at safeguarding the economy rather than reacting to a downturn already underway.* The Federal Reserve lowered rates by 25 basis points at its September meeting and signaled two further reductions this year. The updated dot plot reflected broad support for easing, though views remained dispersed: one projection—widely attributed to new Governor Stephen Miran—called for as much as 125 basis points of additional cuts. Beyond 2025, the dot plot indicated just one reduction in 2026, compared with three cuts priced by markets, and another in 2027, bringing policy rates closer to the 3% neutral level. Roughly six officials penciled in a long-run rate below the median, underscoring a divergence of views on where policy should ultimately settle.

  Within the committee, most of President Trump's appointees supported the decision, with only Miran dissenting in favor of a larger 50bp cut. Chair Jerome Powell stressed that oversized policy moves are typically reserved for situations where policy is badly misaligned, signaling that the current economic backdrop does not warrant such urgency.

  The Fed's policy discussion revealed shifting priorities. Officials appear increasingly less concerned about trade-driven inflation, focusing instead on slowing growth and rising unemployment. Powell pointed to an unusual slowdown in both labor supply and demand, warning that job creation is running below the breakeven rate needed to stabilize unemployment. Tariffs have begun to push up goods prices, but the Fed views these effects as likely temporary. Powell acknowledged tariffs may be contributing to the slowdown but argued labor market weakness is more directly tied to reduced immigration, softer labor force growth, and weakening demand for workers.

  Political pressures also surfaced during the press conference, though Powell continued to draw a clear line on independence. He reiterated that Fed decisions are guided by economic data and long-term objectives, not political considerations, emphasizing the institution's culture of internal debate. At the same time, he declined to comment on Treasury Secretary Scott Bessent's call for an independent review, his own term expiring in May, or Trump's push to remove Governor Lisa Cook, framing them as political or legal matters outside the Fed's remit.

- **CHANGES TO ECONOMIC FORECASTS:** *Fed officials now project the funds rate at 3.6% by year-end, down from 3.9% in June, marking the start of a new easing cycle after last year's 100bp cuts and a pause earlier in 2025.* One more cut is expected in 2026. The median forecast sees the rate at 3.4% in 2026, and 3.1% in 2027, each a quarter point lower than in June. Views within the FOMC remain divided: 18 officials see at least one cut this year, one projects six, and only one expects no change (vs. seven in June), reflecting a more dovish tilt. Powell acknowledged the wide dispersion of views as natural in such an unusual environment.

  Concerns over stagflation persist, with the SEP showing core inflation at 3.1% this year, easing to 2.6% in 2026 and 2.1% in 2027. Unemployment is forecast to rise to 4.5% this year (from 4.3% in August) before gradually edging down to 4.3% by 2027. GDP growth was revised up to 1.6% this year, rising to 1.9% in 2027.

  Near-term risks are skewed—upside for inflation and downside for employment—creating a difficult trade-off. With employment risks rising, the balance has shifted, and the Fed judged it appropriate to move closer to a neutral policy stance. This decision leaves the Fed well positioned to adjust policy as conditions evolve, guided by incoming data, the outlook, and risk assessments.

- **ECONOMIC ASSESSMENT:** *In the near term, inflation risks lean upward while employment risks tilt downward—posing a difficult challenge.* Fresh labor market data highlights mounting economic risks. The U.S. is edging toward a "growth recession" this year, with output running well below potential but avoiding a full downturn—likely pushing unemployment slightly higher. In 2026, growth is set to rebound after a weak first half, supported by stronger capital spending, easing tariff uncertainty, accommodative financial conditions, looser monetary policy, and lingering fiscal support. Inflation should gradually ease next year as tariff-related base effects fade, wage growth stays moderate, and technology-driven productivity gains help contain costs in certain sectors.

  Recent data show that economic growth has slowed, with GDP rising about 1.5% in the first half of the year, down from 2.5% in 2024. The moderation reflects weaker consumer spending, though business investment in equipment and intangibles has strengthened. Housing activity remains subdued. The SEP projects GDP growth of 1.6% this year and 1.8% next year, slightly above June's forecast.

  The labor market is softening: unemployment edged up to 4.3% in August, job gains slowed to just 29,000 per month over the past three months, and labor supply has weakened due to lower immigration and participation. Wage growth is moderating, though still outpacing inflation. The SEP sees unemployment at 4.5% by year-end, easing thereafter.

  Inflation has fallen sharply since 2022 but remains above target. Total PCE rose 2.7% over the past year, with core at 2.9%. Goods inflation has firmed while services continue to disinflate. Near-term inflation expectations have ticked higher on tariff news, but longer-term expectations remain anchored near 2%. The SEP projects PCE inflation at 3.0% this year, 2.6% in 2026, and 2.1% in 2027.

- **OUR TAKE:** *Further cuts ahead.* As discussed in the preview, we expect at least one more cut in December, but clearly the door is wide open for an additional cut in October, depending how economic activity and inflation evolve. The end-point of the easing cycle is likely to be closer to 3% than 2%, but clearly the presence of Miran, Waller and Bowman will become more influential over time and it's possible that Trump's view of significantly lower rates may eventually materialize, even if they were not warranted.

- **MARKET REACTION AND IMPLICATIONS:** *Market reaction to the Fed's first rate cut was muted*. *In the fixed-income space,* the Treasury yields fell after the Fed's first rate cut in nine months, with the 10-year briefly dipping below 4.0% as investors bet lower rates will revive growth. 2-year Treasury yield first fell to as low as 3.47%, but then rose again and now trades around 3.55%. 10-year Treasury yield now trades around 4.08%. *In the currency space,* dollar fell sharply after the Fed's rate cut, with the USD Index down 0.3% at 96.39, on track for its lowest close since February 2022. The greenback is down over 11% this year and facing its worst three-day stretch since July, as investors shift toward markets offering higher returns. *In the equity space,* stocks the Dow rose 0.6% to a record 46,018.32, while the S&P 500 slipped 0.1% and the Nasdaq fell 0.3% after the Fed cut rates as expected. Powell downplayed hopes of a prolonged easing cycle, tempering market enthusiasm. The Russell 2000 added 0.18%, reflecting small caps' greater benefit from lower borrowing costs.