Aegon Asset Management

FOMC UPDATE: THREADING THE NEEDLE

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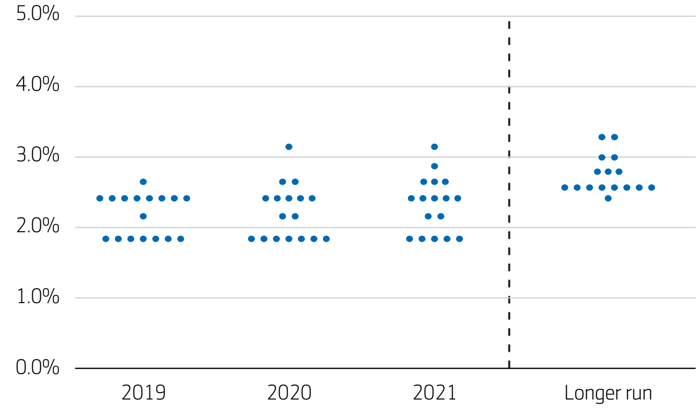
As broadly expected, the FOMC left interest rates unchanged at the conclusion of their June meeting. While the Committee acknowledged the relative softness in recent economic data—it is important to draw attention to the following two statements it made following the meeting: "…uncertainties about [the Committee's economic] outlook have increased." And it also stated: "The Committee will closely monitor the implications of incoming information for the economic outlook and will act as appropriate to sustain the expansion, with a strong labor market and inflation near its symmetric 2 percent objective."

These two points are relevant for a few reasons. First, the FOMC is essentially saying it doesn't think the market is crazy for the increase in economic growth concerns that have accelerated since its May meeting. Second, it did so without overtly calling out the breakdown in US/China trade talks and the increased likelihood of tariffs as a significant reason for this increase in growth concerns. Lastly, by removing the statement "..the Committee will be patient…", it opened the door to cutting rates at any point in time, possibly as early as July—depending on how both the economy and/or US/China trade talks develop.

Overall, this gives the Committee all the latitude it needs to react to future changing developments without necessarily committing to a cut. That said, the Committee did also update its "Dot Plot" of individual Committee members' expectations for the level of the federal funds rate at the end of the next few years. Relative to its March meeting, the dots shifted lower, with the average 2019 dot moving lower by 38 basis points, but the median dot remaining unchanged. The 2020 and 2021 median, however, did shift lower by 38 and 25 basis points, respectively.

Generally speaking, the FOMC appears to have threaded the needle with this meeting. It opened the door to future cuts based on either deteriorating economic data or tariffs, without necessarily committing to a cut outright. This should help give the market an increased level of confidence that the Fed has the market's "back," so to speak, providing some support for both risk assets and curve steepeners in the near future.

Exhibit 1: The Fed's new dot plot



Source: US Department of the Treasury. As of June 19, 2019. Note: Each shaded circle indicates the value (rounded to the nearest 1/8 percentage point) of an individual participant's judgment of the midpoint of the appropriate target range for the federal funds rate or the appropriate target level for the federal funds rate at the end of the specified calendar year or over the longer run. One participant did not submit longer-run projections for the federal funds rate.

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