

# Fed stays put as it tries to get the “timing right” for resuming cuts

Javier Amador, Fátima del Río, Iván Fernández

## Only a significant rise in the unemployment rate would alter the Fed’s “wait-and-see” stance by the time of the September meeting

**The FOMC left rates unchanged at 4.25-4.50%, as widely anticipated, amid unsurprising dissenting votes from Bowman and Waller, who favored a 25bp rate cut.** The statement included a downgrade to the assessment of growth, acknowledging that it “moderated in the first half of the year,” in contrast to June’s assertion that activity had “continued to expand at a solid pace.” This revision followed the release of Q2 GDP data earlier in the day, which showed that final sales to private domestic purchasers slowed to 1.2% from 1.9% in Q1, reflecting resilient but unexceptional consumer spending and subdued private investment—despite a headline 3.0% annualized gain in real GDP that was largely driven by a rebound in net exports after a sharp drag in Q1. The statement continued to describe economic uncertainty as “elevated,” omitting June’s nod that it had “diminished.” This comes amid some progress in trade negotiations with Japan and the Eurozone during the intermeeting period. However, reciprocal tariffs on many other trade partners are still officially scheduled to take effect at the end of this week, on August 1, so uncertainty remains—especially as agreements with major partners such as China, Brazil, and Mexico are still pending—justifying the Fed’s more cautious tone. Thus, while the shift in the activity assessment tilted the statement modestly dovish, the reassertion of elevated uncertainty around tariffs likely aimed to temper any market perception of a meaningful pivot. Despite Bowman and Waller’s recent arguments in favor of a rate cut, their views were insufficient to prompt a surprising third dissent. The forthcoming minutes of “one of the better meetings [Powell] can recall”—due in three weeks—will be key to determine whether other members are beginning to align with their view, but Powell’s comments during the Q&A suggest that’s not the case.

**With inflation running above target and maximum employment right at target, Powell continued to defend a “modestly restrictive” policy stance.** Despite the absence of strong signals of tariff effects in recent official data, Powell stressed that “we have a long way to go to really understand exactly how it will be,” calling it “still quite early days.” Even so, he acknowledged that “a pretty reasonable base case is that this will be a one-time price increase,” but emphasized that the Fed’s priority is to ensure it does not evolve into sustained inflation. Responding implicitly to Waller’s remarks two weeks ago on the case for cutting now, Powell pushed back on the notion that the labor market is “on the edge,” repeatedly affirming that while downside risks are present, “you don’t see weakening in the labor market.” He acknowledged that private sector job creation has come down a bit, but also explained that the unemployment

rate (UR) is still low, and “what that’s telling you is that demand for workers is slowing but so is the supply.” That is, unemployment is being held down because both labor demand and labor supply are slowing down. Thus, it seems that in contrast with Waller’s view, the key labor market variable for the majority of members is still the UR. Softer job creation would not be enough to cut rates if the UR remains steady. He also tried to counter Waller’s claim that inflation would be “quite close” to target if tariff effects were excluded, stating instead that “even if you look through the tariff effects, we think it’s still a bit above target, and that’s why our stance is where it is.” Powell’s key message on the policy outlook was that the Committee is committed to managing the risk of de-anchoring inflation expectations effectively through careful policy calibration, explaining that “we’re trying to get that timing right”—neither easing prematurely nor holding rates too high for too long and risking unnecessary damage to the labor market. He reiterated that no decisions had been made regarding a potential September cut and emphasized the Fed’s independence, noting that policy decisions are guided solely by the dual mandate and are not influenced by fiscal or political considerations.

**A rate cut in September remains a possibility if the labor market proves to be “on the edge” and weakens sharply, but that seems unlikely at this stage.** With Powell emphasizing that the majority view on policy remains unchanged—“inflation is above target, maximum employment is at target, [which] means policy should be a little bit restrictive [...] because we want inflation to move all the way back to its target”—and with two-sided risks to both of the Fed’s goals, we still think it is more likely than not that, after two additional full rounds of inflation and job data ahead of the September meeting, inflation will remain farther from its target, particularly as upward pressures are likely to continue building over the coming months. The framework adopted by the majority of voting members is that, with inflation still at some distance from the target, a “modestly restrictive” policy remains appropriate. If the UR starts to rise, the Fed could come around to the view that the risks to both goals are more balanced—i.e., that both inflation and employment are away from their targets—and “that would imply that policy shouldn’t be restrictive, it should be more neutral.” When that time comes, the Fed will cut rates. However, given that core inflation is likely to rise during the intermeeting period, we remain confident—for now—that a rate cut in September is still unlikely. What could change the odds of a rate cut at the next meeting? A sudden rise in the unemployment rate. For now, we are sticking with our forecast that the Fed will wait until December to resume rate cuts and begin guiding the fed funds rate toward a more neutral level.

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