

## Future Data Will Decide Fed Policy

The September FOMC meeting is a month away and it's increasingly likely committee members will announce the first interest rate cut since March 2020. Inflation has moderated significantly after an unnerving first quarter bump, while the labor market is showing signs of stress. However, the overall economy continues to hold up reasonably well. Diminishing price pressure has given Fed officials latitude to reduce the overnight rate target, but recent data supports a more patient pace than the bond market has priced in.

As of this afternoon, futures are indicating nearly four quarter point cuts before yearend and a total of 200 basis points over the next 12 months. In order for this scenario to play out, the U.S. economy and the labor market would have to weaken and inflation would have to continue its retreat. This is certainly possible, but betting against growth in the post-pandemic era has been a losing proposition.

Last week, the July Consumer Price Index (CPI) rose +0.2% (0.155%), after falling -0.1% (0.056%) in June. Core CPI was also up +0.2% (0.165%), following a +0.1% (0.065%) increase in June. On a year-over-year basis, headline CPI did slip below +3.0% for the first time in three years at +2.9%, but core CPI is rising at a +3.2% rate. Although annual core inflation is also at a three-year low, the pace remains well above the Fed's target and the majority of lingering price pressure continues to be shelter costs, *which actually rose last month*.

Investors considered the July CPI numbers to be acceptable despite month-over-month increases, focusing instead on the extremely soft three-month annualized +0.4% headline and +1.6% core.

The following day, the July retail sales report suggested consumer demand might be picking up again. Overall sales climbed a full +1.0%, well above the +0.4% median forecast and a sharp improvement from the revised -0.2% June reading. The biggest contribution (by far) came from auto sales, which bounced back from the June cyberattack that affected auto dealerships. If auto sales are stripped out, the sales growth rate drops to +0.4%.

When July retail sales figures are considered, the Atlanta Fed's GDPNow real-time measure for the third quarter climbs to +2.0%. The U.S. economy appears solid while inflation is declining, *the classic soft-landing*. Fed policy seems to be working, but growth and prices seldom move in a straight line.

There's quite a bit more data to be collected before September 18th. Committee members will see the August employment report, CPI, retail sales, and July PCE before making their decision. All have potential to reroute policy.

The employment mandate has reemerged as a focal point of Powell and committee members. This adds considerable weight to the August labor report, scheduled for

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release the first Friday in September.

The Fed has opened the door for meaningful easing this year, but the timing and magnitude will be data dependent with an emphasis on employment. An intermeeting cut is off the table, and a 50 basis point move in September (even if the data supports it) is unlikely as the larger move would appear to benefit the incumbent party six weeks before the election.

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## Market Indications as of 3:50 P.M. Central Time

DOW	Down -62 to 40,835 (HIGH: 41,198)
NASDAQ	Down -60 to 17,817 (HIGH: 18,647)
S&P 500	Down -11 to 5,597 (HIGH: 5,667)
1-Yr T-bill	current yield 4.44%; opening yield 4.49%
2-Yr T-note	current yield 3.99%; opening yield 4.06%
3-Yr T-note	current yield 3.79%; opening yield 3.86%
5-Yr T-note	current yield 3.69%; opening yield 3.76%
10-Yr T-note	current yield 3.81%; opening yield 3.87%
30-Yr T-bond	current yield 4.06%; opening yield 4.12%

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