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U.S. ECONOMY

Fed Officials Viewed July Rate Cut as 'Recalibration' of Policy

Central bankers say uncertainty surrounding President Trump's trade policy creates a 'persistent headwind' for economy

By Nick Timiraos

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WASHINGTON—Federal Reserve officials faced divisions over their decision to cut interest rates last month and saw their move as a "recalibration" rather than the start of a more aggressive easing cycle.

The minutes of the July 30-31 meeting, released on Wednesday, also showed officials believed uncertainty surrounding the Trump administration's trade policy wasn't likely to let up anytime soon, creating a "persistent headwind" for the U.S. economic outlook.

As a result, officials didn't spell out in much detail how they might act to lower rates in the months ahead. In July, they voted to cut their policy rate by a quarter percentage point to a range between 2% and 2.25%.

"Most participants viewed a proposed quarter-point policy easing at this meeting as part of a recalibration of the stance of policy, or mid-cycle adjustment, in response to the evolution of the economic outlook over recent months," the minutes said, adding that risks to the economy "highlighted the need for policy makers to remain flexible."

How Fed officials judge the need for further stimulus in the face of trade policy uncertainty is a key focus for investors in the weeks leading up to the Sept. 17-18 meeting. Mr. Powell is set to speak on the challenges facing monetary policy makers at the Kansas City Fed's annual conference in Jackson Hole, Wyo., on Friday.

The minutes showed officials acknowledged markets weren't more volatile in July because investors expected the Fed to cut rates at the meeting that month and at least once more this year. Investors in futures markets have placed a 98% probability on another quarter-point rate cut at the Sept. 17-18 meeting.

Fed officials "seem fully aware that accommodative financial conditions are dependent on their own expectation of cutting," said Michael Gapen, chief U.S. economist at Barclays, which he said suggests another cut is likely at the September meeting.

The minutes showed several officials favored holding rates steady because they judged "that the real economy continued to be in a good place."

Two of those officials, Boston Fed President Eric Rosengren and Kansas City Fed President Esther George, dissented from the decision to cut rates.

Two other officials, not identified in the minutes, favored a more aggressive half-point rate cut, which they said would better address "stubbornly low" inflation rates, according to the minutes. But those officials didn't formally dissent, either because they weren't voting members of the Federal Open Market Committee or because they didn't feel strongly enough about the decision.

While inflation held at the Fed's 2% target for much of last year after falling below that for years, it has again drifted lower this year. Core prices, which exclude volatile food and energy categories, rose 1.6% from a year earlier in June.

Fed Chairman Jerome Powell disappointed some investors at his postmeeting news conference when he pushed back against market expectations of a more vigorous series of rate cuts to follow. Stock markets fell after the July 31 news conference, and recovered the following morning.

"Now we know why Powell had a hard time at the press conference. There wasn't a clear consensus," said Diane Swonk, chief economist at Grant Thornton.

Ms. Swonk said the committee appeared split between traditionalists who believe the Fed should focus most of its attention on the domestic economy and a new guard that thinks they must be more attentive to global conditions because greater linkages in trade and financial markets increase the potential for spillovers from other economies.

Markets plummeted again on Aug. 1 after President Trump said he would impose 10% tariffs on $300 billion in Chinese goods later this year that weren't already subject to tariffs.

That escalation, together with reports of weaker activity in Germany, China and other countries dependent on trade, set off a series of volatile moves in bond markets. Yields on the 30-year Treasury bond fell briefly below 2% last week for the first time ever.

The Fed has been under unusual and sustained public criticism from Mr. Trump, who called on Mr. Powell to cut rates more aggressively on Wednesday morning, for the third consecutive day. "He's like a golfer who can't putt, has no touch," Mr. Trump tweeted.

Fed Chairman Jerome Powell and the central bank's monetary policy have been frequently criticized by President Trump.
PHOTO: JIM LO SCALZO/EPA/SHUTTERSTOCK

Ms. Swonk said the divisions over whether to cut rates "illustrate how little influence the president's words have had on the Federal Reserve."

Fed officials say they don't discuss politics at their meetings, but the minutes show how officials have grown more concerned about businesses freezing planned investments due to the uncertainty caused by the president's trade policies.

Trade-related developments in the run-up to the July meeting had been slightly positive relative to market expectations, with President Trump and Chinese President Xi Jinping agreeing to resume trade talks at the G-20 summit of world leaders in Japan in late June.

But officials "were mindful that trade tensions were far from settled and that trade uncertainties could intensify again," the minutes said. "Continued weakness in global economic growth remained a significant downside risk."

Because both the trade and global growth outlooks have worsened since the July meeting, "that formulation suggests they're prepared to cut again" in September, said Mr. Gapen.

The minutes revealed a greater split over the inflation outlook. While some officials thought weaker growth abroad and trade tensions between the U.S. and other countries would push the Fed farther away from reaching its 2% target, many others weren't as concerned, the minutes said.

This larger group of officials believed that recent inflation data suggested that lower readings earlier this year were likely to be temporary, which would remove one of several reasons that compelled last month's cut.

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