



## Natalie Gallagher

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provides a personal view  
on topical economic issues

*“We have revised our unemployment forecast from 4.2% to 4.4% for the coming months. This reflects the growing evidence of labor market slack, which could necessitate further monetary easing to avoid a deeper downturn in employment.”*

# September 2024 Economic Outlook: Fed Pivot! 50 basis point cut to counter labor concerns amid lingering inflation fight

## Key takeaways:

- **Interest Rate Cut:** The Federal Reserve cut interest rates by 50 basis points in September, marking a shift from prioritizing inflation control to focusing on labor market stability. The cut demonstrates confidence in the downward trend of inflation, with an implicit acknowledgment of economic weakening, particularly in employment.
- **Revised Projections by Prevedere:** Prevedere has revised its projections for the U.S. economy in light of recent developments. We now expect an increase in the unemployment rate and anticipate further reductions in the Federal Funds Rate. Specifically, Prevedere forecasts additional 25 basis point cuts in both November and December, leading to a cumulative 100 basis point reduction by year-end.
- **Challenges for the Federal Reserve:** The Fed faces a dual challenge of preventing further labor market deterioration while guarding against inflationary pressures, especially in housing. With monetary policy adjustments exhibiting delayed effects, the Fed's gradual approach is risky in an unpredictable economic environment.

In a notable development last week, the Federal Reserve implemented a 50 basis point cut to the Federal Funds Rate [1], marking the central bank's first reduction since March 2020. This substantial cut signals a key pivot in monetary policy, with the Fed shifting focus from its aggressive inflation-fighting stance to addressing emerging concerns in the labor market.

The move also reflects increasing confidence that inflation is trending downward towards the Fed's long-term target of 2%. However, the decision illustrates the central bank's delicate balancing act: navigating between mitigating

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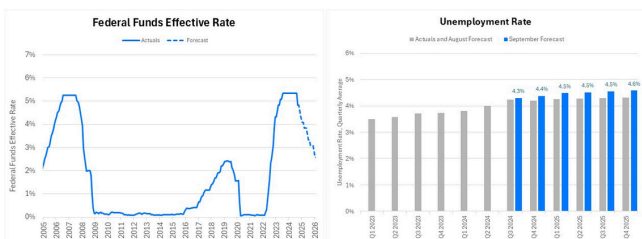
[1] Federal Funds Rate: The interest rate at which depository institutions lend reserve balances to other depository institutions overnight, on an uncollateralized basis. It serves as a benchmark for various other interest rates in the economy.

further labor market weakness and ensuring inflation does not reignite, particularly in areas like housing.

## Context and Implications of the Rate Cut (and dissenting opinions)

The decision to reduce interest rates by 50 basis points comes at a critical juncture, marking a departure from the aggressive tightening seen over the past 18 months. Since the onset of inflationary pressures in 2021, the Federal Reserve has raised rates in an effort to slow demand and bring inflation under control. However, the 50 basis point reduction signals a shift towards addressing concerns over the labor market's strength, particularly as the Unemployment Rate [2] has begun to show signs of softening.

### Navigating the Fed's Balancing Act: Fed Funds Rate Cut and Labor Market Dynamics



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Interestingly, this decision saw the first dissenting opinion from within the Federal Reserve Board since 2005. Governor Michelle Bowman advocated for a smaller, 25-basis point cut, emphasizing the ongoing debate within the

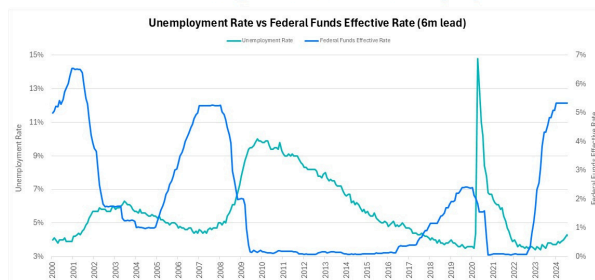
[2] Unemployment Rate: The percentage of the total labor force that is unemployed and actively seeking employment during a given period. It is calculated by dividing the number of unemployed individuals by the total labor force and multiplying by 100.

over the pace and magnitude of monetary easing. Her stance suggests that while the labor market concerns are pressing, some members remain cautious about the inflation outlook, indicating a divergence of opinions within the central bank.

## Leading Indicator Spotlight

Prevedere has downgraded its expectations for the Federal Funds Rate, now forecasting an additional 25 basis point cut in both November and December. Should these cuts materialize, the total reduction for 2024 would amount to 100 basis points, representing a significant easing of monetary policy within a relatively short period.

### Fed Funds Rate: A Leading Indicator for Unemployment



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A critical consideration is the inherent lag in monetary policy effects. Prevedere predicts that, with regard to the Federal Funds Rate, the impact on the Unemployment Rate will be seen 6 months later.

This delay heightens the risks for the Fed, as the full effects of previous decisions, such as holding rates steady in July, may not yet be fully evident in the labor market or inflation data.

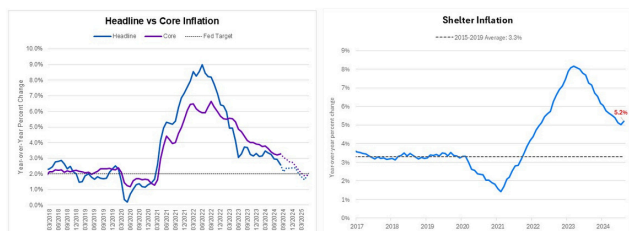
## Ongoing Inflationary Concerns, Particularly in Housing

Chair Powell emphasized that achieving the headline inflation target [3, 4] remains an ongoing challenge. This is a key consideration for Prevedere, as the Federal Reserve faces a particularly nuanced situation due to housing inflation [5] concerns, which accounted for 74% of last month's inflation increase.

Overly aggressive rate cuts could stimulate the housing market via reduced mortgage rates, potentially reigniting inflation concerns.

The Federal Reserve must carefully balance preventing labor market deterioration while avoiding a resurgence of inflationary pressures.

### Inflation Pressures and the Fed's Dilemma: The Challenge of Rate Cuts in a Complex Economy



This task is further complicated by the long and variable lags in monetary policy transmission. If the Fed has already misjudged the state of the labor market by not cutting rates in July, the effects of that decision will already be influencing labor market dynamics for the coming

[3] Headline Inflation: A measure of the total inflation within an economy, including all items such as food and energy prices. It reflects the overall increase in the cost of living but can be more volatile due to fluctuations in food and energy costs.

[4] Core Inflation: A measure of inflation that excludes certain volatile items, primarily food and energy prices, to provide a clearer picture of the underlying inflation trends in an economy. It is often used by policymakers to gauge long-term inflationary pressures.

[5] Shelter Inflation: The portion of inflation that relates to the cost of housing, including rent, homeowners' equivalent rent, and other housing-related expenses. It is a significant component of the Consumer Price Index (CPI) and has a large impact on overall inflation figures.

quarters. This concern was likely a key consideration in opting for a more aggressive 50 basis point rate cut in September, rather than a more conservative 25 basis point reduction.

The Fed's strategy moving forward will be heavily dependent on both unemployment figures and CPI data, which Prevedere anticipates will set the stage for additional rate cuts in November and December. However, given the outsized impact of shelter inflation, the Fed is navigating a precarious balance. The task is particularly challenging because economic conditions can shift rapidly, while the Fed's policy adjustments are inherently gradual - making the risk of a misstep all the greater.

## Outlook and Predictions

In response to these developments, Prevedere has adjusted its own economic projections. Following the release of the August jobs report, which highlighted continued softening in key labor market indicators, we have revised our unemployment forecast from 4.2% to 4.4% for the coming months. This reflects the growing evidence of labor market slack, which could necessitate further monetary easing to avoid a deeper downturn in employment.

## Q&A

*Q1: What can businesses do to proactively navigate this economic environment?*

### 1. Prepare for Debt Refinancing Opportunities

Businesses should begin reviewing their current debt structures, particularly those with upcoming maturities in 2025. The anticipated further reduction in interest rates

presents an opportunity for refinancing, potentially resulting in significant long-term savings on borrowing costs.

## 2. Reassess Hiring and Wage Strategies

With unemployment expected to rise, businesses should reassess their workforce strategies. This may involve recalibrating hiring plans, optimizing wage costs, and focusing on retaining key talent,<sup>3</sup> even as labor market conditions soften.

## 3. Review Pricing Strategies

As the labor market weakens and consumer demand shifts, businesses should conduct a thorough review of pricing strategies. This will enable them to remain competitive and responsive to changing economic conditions.

*Q2: What should be the key focus for businesses to remain resilient in the coming months?*

**Flexibility is Crucial.** Businesses need to be prepared to adapt quickly to economic changes. While the overall outlook may be settling in some areas, the environment remains highly dynamic. Companies should maintain flexible strategies that allow them to pivot quickly in response to new developments.

# Thank you

*These insights were enabled by  
Prevedere's Advanced Predictive  
Planning Platform. For more  
information, click [here](#).*

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