Global Macro Research

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#US / #Monetary policy / #Inflation

Fed cuts 25bps and dots project two more cuts this year

The Federal Reserve lowered rates by 25bps to 4-4.25%. The median dot shows 50bps of further cuts this year, amid rising risks to employment. There was a wide range of views on the committee, including Miran's dot pointing to 125bps of additional easing this year (and a dissent for 50bps today), but the growth and inflation forecasts and Powell's presser moderating the dovishness somewhat.

Key Takeaways

- The Federal Reserve cut rates 25bps to 4-4.25% and the dots point to a further 50bps of easing this year.
- New Board Member Stephan Miran voted for a larger 50bps cut. And the dot plot reflected a range of views about the subsequent path. At one end of the spectrum, what's clearly Miran's "dot" expects another 125bps of cuts this year, while at the other end there is a dot calling for a rate *hike*. The median dot expects an additional cut in both 2026 and 2027.
- The other forecasts showed both the inflation and growth projections were revised slightly *higher*, and unemployment marginally *lower*.
- But Chair Powell made clear that the FOMC sees the balance of risks around the dual mandate having shifted, with a rapid softening in the labour market now balancing out still-elevated price pressures, requiring a more neutral monetary policy stance.
- Powell was quick to shut down questions about encroachment on Fed independence, and markets are happy to interpret easier monetary policy as a broad tailwind for many asset prices. But we remain attentive to politicisation risks, and think it's worth tracking carefully growing talk of the Fed's "third mandate" to secure low long-term borrowing costs.

Fed restarts its cutting cycle

The Federal Reserve (Fed) cut the target for the fed funds range rate by 25 basis points (bps) to 4.0%-4.25%. This was in line with our own and the market's expectations.

The decision was near-unanimous, with only one dissenter: the newly sworn-in Stephen Miran, who preferred a jumbo cut of 50bps.

It was somewhat of a surprise not to see more votes for a larger cut, given that Board Members Christopher Waller and Michelle Bowman were dovish dissenters at the July meeting and have been advocating for a looser monetary policy stance in recent months.

Dovish changes to the dot plot

Going into this FOMC meeting, the big question was not whether the Fed would cut in September, but how big that reduction would be and what it would signal for the two remaining meetings in 2025.

In the updated Summary of Economic Projections (SEP), the median expectation for the fed funds rate (the median "dot") at the end of 2025 was 3.75% to 4.0%, implying 50bps of additional cuts this year (see Figure 1). This would mean consecutive rate cuts at the October and December meetings.

However, the margin was very narrow, with 10 members seeing two or more additional cuts. This includes what is almost certainly Miran's dot incorporating 125bps of additional rate cuts – implying his preference would have been for 50bps of easing today and then the same again in October and December – and nine members seeing one or fewer additional cuts (including one non-voter whose dot implies a rate *hike*).

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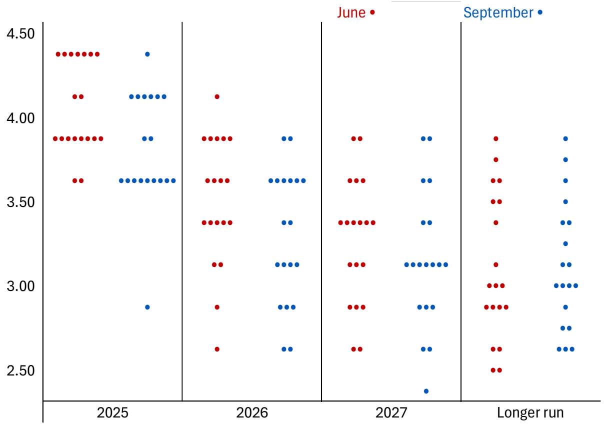
The median projections for end-2026 and 2027 were also lowered by 25bps, to 3.375% and 3.125% respectively.

Figure 1: Projections for the Federal funds rate have shifted lower



Source: Aberdeen, US Federal Reserve, September 2025

But growth and inflation revisions could be interpreted slightly hawkishly

On the other hand, the revisions to the growth and inflation projections were actually *upwards*, and the changes to the unemployment forecasts fractionally downward.

For example, the median official sees Q4 year-over-year GDP growth at 1.6% in 2025, then 1.8%, 1.9%, and 1.8%. Core PCE inflation is seen as 3.1% in Q4 2025, then 2.6%, 2.1%, and 2.0%. The unemployment rate is seen as peaking at 4.5% this year, before then creeping lower again over subsequent years.

An insurance cut as the balance of risks around the dual mandate has shifted

Chair Jay Powell reconciled today's rate cut with these upward revisions to the growth and inflation forecasts by arguing that the balance of risks around the Fed's dual mandate had shifted.

Policymakers face an unusual situation of rising inflation and a softening labour market. But whereas earlier in the year the risks were clearly titled towards higher inflation, the significant slowdown in payroll job growth means that these risks are moving much closer to balance.

We've highlighted previously how slowdowns in the labour market can become increasingly self-fulfilling, as "stall speed" dynamics kick in.

Meanwhile, core goods inflation is showing increasing signs of a tariff-driven pickup and we think core services inflation is still looking somewhat sticky. But, with most measures of long-run inflation expectations still under control, there are reasons to think the rise in inflation will be moderate (at least compared to the post-pandemic overshoot) and temporary.

Hence, another step towards a more neutral policy stance is appropriate.

This position was reflected in the SEP responses on risks to their projections for inflation and the labour market. The number of participants saying risks to the unemployment rate were weighted to the upside increased marginally since June, from 14 to 15. A greater number now assess the risks to headline and core PCE inflation as being broadly balanced compared with three months ago.

Admittedly, Powell did underline that a significant proportion of the slowdown in the growth of payroll employment is being driven by a reduction in the supply of labour, as net migration has dropped dramatically. In line with our own estimates, Powell thinks the "breakeven" rate of monthly payroll growth is as low as 0 to 50k per month, relative to a three-month average gain of 29k.

But, with the unemployment rate ticking up slightly, labour demand is running slightly below this reduced level of supply, presumably due to the impact of tariff uncertainty and the still-tight stance of monetary policy.

More questions on the "third mandate"

Notably, Powell was asked about the oft-ignored third aspect of the Fed's mandate, moderate long-term interest rates.

As we highlighted after the previous Fed decision, the Federal Reserve Act states that the Fed's objectives are "to promote effectively the goals of maximum employment, stable prices, and *moderate long-term interest rates*" (our emphasis).

The long-standing convention has been to think that targeting the first two objectives (the dual mandate) creates the conditions for interest rates to settle at moderate levels. But Miran has started to highlight this "third mandate", including in his congressional hearings to be appointed to the FOMC.

All this raises the possibility – still remote – that the Fed over time becomes increasingly involved in setting longer-term bond yields, *in extremis* through financial repression and yield curve control.

We are forecasting back-to-back cuts this year, and two more in 2026, to a 3% terminal rate

Our forecast is for the fed funds rate to be lowered by 25bps again in October and December, and then twice in 2026, to a terminal rate of 3-3.25%. This is a slightly quicker pace of easing than in the dots, but slightly slower than the pace priced into markets.

Authors:

Jon Butcher & Paul Diggle

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