The case for a December Fed pause

Neil Irwin
December 13, 2024

Financial markets and Fed watchers view an interest rate cut next week as a near certainty. There are some reasons to think the cut might be a mistake.

Why it matters: The case for pausing interest rate cuts is that the inflation outlook has grown murkier, while growth has remained robust in the last couple of months. Risk management concerns, in this argument, tilt toward patience.

- The widespread expectation, however, is that they will move forward with a rate cut next week, then pause rate cutting at the following meeting in late January.
-
- CME's FedWatch tool, based on futures prices, shows almost 97% odds on a rate cut at the Fed policy meeting concluding Wednesday.
-

Flashback: At the Fed's September policy meeting, the median official anticipated two more rate cuts would be justified in 2024. The committee made one such move in November, so an additional rate cut next week would match that forecast.

Yes, but: The economic data has not evolved as officials anticipated three months ago — and both the inflation and job market data have moved in ways that argue for less rate cutting.

- In September, officials anticipated the unemployment rate would average 4.4% in the fourth quarter. It averaged 4.2% in October and November.
- Back then, officials saw 2.6% core PCE inflation in 2024; as of October, that was running at2.8%.
-

What they're saying: "There's now a credible argument to be made why [Fed chair] Jerome Powell and his colleagues should take no action next week and step aside to better understand the inflation dynamics at work," wrote **Bernard Baumohl,** chief global economist at The Economic Outlook Group, in a note.

- "Every major inflation metric lately has pivoted back up and done so with the kind of bias that should unnerve the Fed," he added.

- "I think a rate cut next week will prove to be a mistake because (a) it isn't warranted and may backfire to fuel more inflation, and (b) it risks eroding Fed credibility," said **Baumohl**.

- "Financial conditions have eased and we are on firmer footing than we were when the Fed first cut, at least in terms of overall growth," KPMG chief economist Diane Swonk tells Axios, saying she would opt not to cut rates next week.

Between the lines: In terms of risk management, if the Fed were to skip a December rate cut and then decide it needs to move rates lower in 2025, it has eight policy meetings at which it could do so.

- But if it cuts rates next week and comes to regret it because inflation progress stalls out, it would be more awkward to reverse course and hike rates.
-

The other side: The fact that markets have so fully priced in a December rate cut — precisely because Fed officials didn't do anything before their customary media blackout to push against it — means a surprise could prove disruptive.

- And the November jobs numbers pointed to a softening in the job market, as unemployment rose and Americans dropped out of the labor force.

###