Mixed signals on rate cut prompts Trump to demand the Fed enlist in US trade war against rivals

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The US Federal Reserve has landed itself in controversy and confusion over how much it will cut interest rates at the meeting of its Federal Open Market Committee (FOMC) at the end of this month. The turmoil arises from the fact that as it moves to implement Wall Street's demands for a further boost to financial markets, the Fed is trying to maintain the fiction that it acts "independently."

The markets had priced in a rate cut of 0.25 percent after Fed Chairman Jerome Powell indicated in testimony to Congress earlier this month that the central bank was moving to a more "accommodative" policy in light of concerns over global growth, the impact of the US trade war against China, low US inflation and a fall in business investment.

But in a speech on Thursday, Federal Reserve Bank of New York President John Williams set the financial hares running when he seemed to indicate that the rate-cutting could go beyond expectations. Speaking to the annual meeting of the Central Bank Research Association, he likened early monetary policy easing to vaccination for children to guard against future illnesses. "It's better to deal with the short-term pain of a shot than take the risk that they'll contract a disease later on," he said.

In a clear pointer to bigger-than-expected rate cuts, he said policymakers should not keep their "powder dry" and ease monetary policy only after there was more hard evidence of a downturn. "When you only have so much stimulus at your disposal, it pays to act quickly to lower rates at the first signs of economic distress," he declared.

This orientation was underscored by the remarks of Fed Vice-Chairman Richard Clarida in an interview on Fox Business Network. He said a mostly rosy economic picture should not prevent the Fed from easing its monetary policy.

Clarida has previously approvingly cited examples from 1995 and 1998 when the Fed took out an "insurance policy" and cut rates before there were indications of a downturn. "You don't have to wait until things get so bad to have a dramatic series of rate cuts,"

he said. "You don't want to wait until the data turns decisively if you can afford to."

There was a significant market reaction to Williams' remarks. The yield on US Treasury bonds fell and investors priced in a 66 percent chance of a rate cut of 0.5 percentage points (50 basis points) at the end of the month, compared to a 40 percent chance before he spoke.

The New York Fed then decided to intervene, with a spokesman issuing a statement cautioning against reading too much into its president's remarks. "This was an academic speech on 20 years of research. It was not about potential policy actions at the upcoming FOMC meeting," the statement said.

Academic speech or not, Williams and others would have known full well the impact of his remarks just days before the cut-off point for public comment by Fed officials in the lead-up to the FOMC meeting.

As Neil Dutta, head of economics at Renaissance Macro Research, said in a note to clients: "We have not seen anything like this before and honestly, we are not sure what they were thinking. Of course the market would latch on to a speech like this—given the focus and timing—right before the July confab."

David Rosenberg, chief economist at Gluskin Sheff, a wealth management firm, said: "I think we have too many cooks in the kitchen when it comes to public speaking at the Fed, and it's sowing seeds of confusion."

But more is involved than the number of voices. The turmoil and confusion are a product of the intense pressure from Wall Street for still more cheap money to boost the markets even beyond their present record levels.

The New York Fed's intervention appears to have been motivated by concerns that Williams' remarks, had they been allowed to stand, would have all but locked the Fed into a 50 basis point cut at the end of the month out of fear that anything less might "spook" the markets, thereby tearing away what remains of the fiction that it acts independently.

US President Trump intervened, as could be expected, given that he has issued strident demands that the Fed cut rates and boost Wall Street by a further 10,000 points on the Dow.

In an initial tweet, issued after the intervention by the New York Fed, he said: "I like New York Fed President John Williams' first statement much better than his second. His first statement is 100 percent correct in that the Fed 'raised' far too fast and too early."

In a later tweet, he added a new component to his attack on the Fed, indicating that it should become more closely aligned with the global economic warfare being waged by the US administration.

While China is the most publicly visible focus of this war, it is by no means the only target. Trump has pointed to the monetary easing policy of the European Central Bank as leading to a fall in the value of the euro to the detriment of the US, and returned, at least indirectly, to this theme in his comments on the Fed.

"Because of the faulty thought process we have going for us at the Federal Reserve, we pay much higher interest rates than countries that are no match for us economically," he tweeted.

Calling for an end to what he called "crazy quantitative tightening," Trump tweeted: "We are in a world competition and winning big… but it is no thanks to the Federal Reserve." Had they not acted so fast and so much, he continued, "we would be doing even better than we are doing right now."

In other words, the demand of the Trump administration is that the Fed should not only juice Wall Street at home, in order to further siphon wealth into the hands of the financial elite, but must directly function as a US weapon in the global war against Washington's economic rivals.