Rate Cuts Really a Tonic for Stocks?

By all but promising a rate cut at the end the day, Chair Powell's congressional testimony sent equities and other risk assets higher. The promise of a easier policy seemingly just what the market craved.

However, a little history might make investors take a more circumspect look at the market environment. Today's chart of the behavior of the S&P 500 around Fed easing cycles shows that on the eve of such changes in policy, loading up on stocks is not a winning play.

On this score, a read of the minutes of the June FOMC might be in order as well. Although likely overshadowed by the live testimony, the depth and breadth of the FOMC's concern expressed in the minutes about trade and other policy uncertainties and the downside risks to the economy (along with stubbornly low inflation and inflation expectations) is striking.

While it is often an article of faith of that "the Fed reacts to the equity market", the fact is that equities usually underperform at the beginning of easing cycles and it's more likely that what causes the Fed to cut rates (weak growth, rising financial risk) drags equities down with policy rates.

The minutes and the Powell testimony on the Hill today clearly indicate that we're close to that point.

Federal Funds Rate and S&P 500
Federal Funds and US Equities

SOURCE: BNY Mellon Markets, Bloomberg, data through 9 July 2019

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