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October 29, 2025

Fed announcement: Tensions between the goals and the committee

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The FOMC cut its policy rate today as expected, and is also ending its balance sheet drawdown on December 1st. A couple of dissents on the monetary policy side, with Governor Miran favoring a 50bps cut and KC Fed President Schmid voting for a hold. There were a few changes in the statement that suggest the Fed is looking towards soft data to gauge the health of the economy and the job market.

The big takeaway of today's press conference is that a December move is a maybe, with the market now paring rate bets from a sure thing to about a two-thirds chance as of writing. The main reason for that was Powell's more measured tone that came as the result of both the data fog, but also a weaker macro case. The labor market is moderately cooling, we have "bifurcated" yet strong economic activity, and the higher neutral estimates have some committee members drawing the line and calling for at least a pause.

We've long seen the merits in that view and have been expecting the Fed to pause in December, on those arguments raised within the committee, and also because we're not so confident that inflation can return to target with policy at or slightly below neutral. There does seem some part of price pressures driven by demand, even if it has diminished, it's warranted to keep policy somewhat restrictive in real terms to prevent expectations from loosening up too much. If the shutdown persists or we're unable to get enough meaningful data ahead of the next FOMC meeting, a December pause would seem more likely than not.

The focus on December misses the bigger picture. There is a growing tension between the Fed's goals, and also likely within the committee, that is going to be more apparent as the effect of the trade war become more evident on the economy and prices. We saw two opposing dissents today and its not unreasonable to expect more of that as we go along, particularly if tariff pass-through rises on major durable goods items like cars and that spills over into service prices like car insurance and maintenance.

More disagreements will mean compromise and possibly a less linear, and slower path to neutral -- at least until a new chair is installed. Our view is the Fed pauses in December and cuts two more times in the next year.