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# Less is more?

***The Federal Reserve cuts short-term interest rates by 25 basis points and indicates that there could be more to come, if necessary.***

In a much-anticipated move, the Federal Reserve reduced short-term interest rates for the first time since the financial crisis began over a decade ago. The decision by the FOMC was described by Fed Chair Jay Powell as, insuring against downside risk, and uncertainties from a weakening global economy, continuing trade tensions between the US and China, as well as persistently low inflation. The 25-basis point reduction in short-term rates had been well telegraphed to the capital markets, although some market participants were calling for (hoping for) a 50-basis point cut. For now, a one quarter-point rate cut seems to be a compromise between those at the Fed who wanted to get ahead of any global economic weakness and those who saw little need to ease rates at present.

In some respects, the game on Wall Street is to observe both what the Fed does as well as what they say, in order to seek to understand the tenor of Fed policy action as being dovish, neutral or hawkish. This has led to some amusing capital market oxymorons, such as dovish–hike or hawkish–cut, among others. It seems as though the markets may have originally interpreted the Fed's move as a hawkish-cut and in the immediate aftermath equities declined, the yield curve flattened, credit spreads widened, and the U.S. dollar strengthened to an 8-month high. In fact, at one point yesterday, the U.S. Treasury yield curve briefly touched a spread between the two-year and the ten-year of just 11 basis points, which was the flattest the yield curve has been since 2007. All else being equal, a flattening of the U.S. Treasury yield curve can be a signal that fixed-income investors believe that the central bank may be pursuing a policy agenda that is too tight. It appears that at least for now, the bond market is betting that this interest-rate cut by the Fed will not be their last.

## Global Competitive Currency Devaluation

With the Fed's rate cut, the U.S. dollar rallied as traders bet that a U.S. Fed that is less dovish than the world's other major central banks will mean continued U.S. dollar strength, at least for the time being. A stronger U.S. dollar has the de-facto effect of tightening monetary conditions around the globe since it is the world's funding currency. However, the Fed's decision to lower short-term rates yesterday may be their first move in an ongoing global competitive currency devaluation among the world's central banks.

## Trump Increases Tariffs on China

Then, as if on cue, following the Fed's announcement, President Trump abruptly escalated his trade war with China, announcing that he would impose a 10% tariff on $300 billion in additional Chinese imports, beginning on September 1st. With this announcement, the Trump administration has now broken off from the tentative trade cease-fire between the U.S. and China. Plus, the 25% tariff already imposed on $250 billion in Chinese goods will remain in place. It is widely believed that the list of targeted goods could include many consumer and technology products, including most of Apple's major products such as the iPhone. While there is still time to negotiate, fundamental disagreements remain at this point, and even the threat of tariffs could take a severe toll on business confidence, business investment, and global growth going forward. By escalating U.S. China trade tensions, President Trump may also be seeking to put additional pressure on the Fed to consider further rate cuts in order to avoid an economic slowdown.

## Potential Shift in Market Psychology

It is also possible that the recent move by the Fed combined with the Trump administration's announcement regarding additional tariffs on Chinese goods could usher in an eventual shift in investor psychology. In the recent past, weaker economic activity was somewhat perversely seen to have been a positive for equities, because it meant that central banks would continue to add liquidity to the system. However, going forward, it may be the case that weak economic data and escalating trade tensions may begin to overwhelm any additional liquidity coming from the Fed and the world's other major central banks. Market psychology may be starting to shift towards a perception that the Fed is once again behind the curve in easing monetary policy, and this could spark fear among investors that the global economic slowdown may gather momentum and be exacerbated by increased trade tensions between the U.S. and China.

## Our View

Here at EisnerAmper Wealth Management, the recent move by the Fed and the Trump administration's announcement concerning additional tariffs has not changed our overall outlook for the global capital markets. We still see the U.S. equity market as fair valued, emerging market equities are somewhat undervalued (although they may struggle in the short-term if the U.S. dollar strengthens), and we continue to believe that using some alternative investment strategies could be the best hedge during a period of global currency devaluation among the world's major central banks. Based upon our research and decades of experience in managing portfolios, we continue to believe that it is appropriate to remain in a somewhat defensive posture towards portfolio allocations as the risk of a correction in the equity markets continues to increase. However, this is not to say that we will be entirely out of the equity markets now or in the future since we know from history that there could be equity market rallies which we may seek to take advantage of along the way.

We will continue to conduct our research into the significant economic and behavioral forces which may drive markets either higher or lower from this point and continue to prioritize risk management and seek to limit potential portfolio drawdowns.

As always, please feel free to reach out to us at any time if you have questions or comments.

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***As always, information provided should be considered based on your personal needs to accomplish your goals. At EisnerAmper, we will be happy to discuss with you any questions and how these principals can be applied to meeting your financial plan. Feel free to contact Marc Scudillo, Managing Partner of EisnerAmper Wealth Management & Corporate Benefits, LLC; 908-429-0025 or email at mscudillo@eawmcb.com.***

**Disclosure**

or sector.

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