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September Rate-Cut Path Gets Clearer

BY NICK TIMIRAOS

The July jobs report could give Federal Reserve officials a sense of déjà vu.

Last year, officials decided against cutting interest rates at their July policy meeting, but an employment report two days later suggested the labor market wasn't as strong as it looked. Officials made up for it by cutting rates by a half-percentage point, larger than the traditional quarter point increment, at their subsequent meeting in September.

This past week, officials also held rates steady, only to wake up Friday to news that the labor market unexpectedly cooled during the past few months. Traders increased the chances of a September rate cut to more than 70% from 38% Thursday.

The situations aren't exactly the same, of course. Last year, inflation was heading lower. This year, officials are worried that price pressures could pick up due to broad increases in tariffs that have been going into effect since the spring.

The latest jobs report shows how a series of policy experiments in the early months of the Trump administration could be slowing the economy and labor markets. They include a crackdown on immigration that could reduce the number of people available to work, an increase in tariffs that might damp demand, and job cuts for federal workers and other contractors and nonprofits that rely on government partnerships.

White House advisers earlier this year warned the economy might go through some shortterm pain, or a "detox period," as they implemented the president's campaign promises. Congress also approved last month Trump's signature tax-cut package.

A key question for the Fed will be whether the underlying economy is weakening or whether the recent slowdown reflects the lagging but temporary effects of certain other policy changes. ?

The big news in Friday's report was that job growth for May and June was revised sharply lower. The slowdown in hiring through the middle of the year opens the door wider to a rate cut at the Fed's September meeting, though the Fed has plenty of time to decide. Officials will have one more employment report before that gathering and two more months of inflation data.

At a minimum, the July jobs report underscores the highwire act they face as the economy appears to be cooling down at a time when price pressures are firming up. The Fed has been concerned about such a scenario since March, when President Trump began announcing larger increases in tariffs.

Fed officials have said they are putting less emphasis on headline job growth because it has been declining alongside less growth in the labor force. When the supply of workers declines, the unemployment rate can hold steady or fall even if job growth slows. The unemployment rate ticked up to 4.2% in July from 4.1% in June.

Still, Fed Chair Jerome Powell this past week said the unemployment rate's stability could mask underlying weakness. That is because when fewer people seek work at the same time that fewer jobs are available, the resulting equilibrium is inherently fragile.

Powell referred six times at a news conference to "downside risks" in the labor market, suggesting that realized weakness could build a case for easing policy.

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“You don’t see weakening in the labor market, but I think you’ve got downside risks in a world where unemployment is being held down because both demand and supply are declining,” Powell said on Wednesday. “It’s worth paying close attention to it. And we are.”

Two Fed governors, Michelle Bowman and Christopher Waller, dissented from the decision to hold rates steady on Wednesday, preferring to have lowered rates by a quarterpoint. In separate statements released Friday morning, they both pointed to the risk of a weaker labor market in calling for the Fed to resume rate cuts that policymakers suspended at the beginning of the year.

Fed governor Adriana Kugler announced Friday that she plans to resign from her post next week. Her term as governor was set to expire early next year. The vacant seat opens a slot for Trump to place his own nominee on the Fed board.

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