

March 3, 2020

Fed takes extraordinary action in response to coronavirus fears

- Fed cut rates by 50 basis points this morning
- First action between meetings since October 2008
- Volatile reaction in equity markets while 10-year Treasury yield hits new low

The Fed took extraordinary action this morning to address what it called "evolving risks to economic activity" related to the coronavirus outbreak. The decision to lower the fed funds target range by 1/2 percent was unanimous. A move of this size, at or before the committee's next meeting on March 18, was already fully priced in financial markets after a statement from Chair Powell late last week suggested the Fed was ready and willing to take action. Today's statement echoed Friday's, saying the central bank is "closely monitoring developments and their implications for the economic outlook and will use its tools and act as appropriate to support the economy." However, at a press conference following the decision, Chair Powell didn't hint at any further policy changes (rate cuts or otherwise) and said the committee likes its current stance.

The Fed's rate cuts followed this morning's call with G7 finance ministers and central bank governors that failed to deliver any concrete, coordinated action. Equity markets were under downward pressure after the G7 announcement, and the Fed's unilateral move only provided temporary relief. Powell noted that monetary policy is only one facet of the required policy response, with health authorities and fiscal policy also needing to play a role. While lower rates "won't fix a broken supply chain," today's move is meant to "avoid a tightening in financial conditions" and "help boost household and business confidence."

Our forecast is for the Bank of Canada to lower its overnight rate by 25 basis points tomorrow and again in April. Today's announcement by the Fed raises the odds that the BoC lowers rates by 50 basis points in one go. However, we still think it's more likely that the BoC follows the RBA's lead from last night, announcing a 25 basis point cut and leaving the door open to further moves.

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