US data still supports further Fed cuts. (UBS)

Look for cash alternatives as interest rates fall further

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US equities last week gave up more than half of their gains following the US election, with the S&P 500 falling 2.1% on concerns that the Federal Reserve may pause its easing cycle in the year ahead.

October's inflation and retail sales data came in above consensus, while Fed Chair Jerome Powell signaled that the central bank was in no hurry to lower rates. Separately, data showed that total assets in US money market funds rose above USD 7tr last week for the first time.

But we continue to believe that cash and money market holdings should be limited to cover one year of spending needs, as cash returns will diminish alongside the global rate-cutting cycle that we believe has further to go.

US data still supports further Fed cuts. Last week's inflation data suggest that the personal consumption expenditures (PCE) price index, the key inflation gauge for the Fed, should rise in October, while retail sales readings showed solid consumer spending. However, retail sales excluding autos and gas increased just 0.1% in October, below the consensus forecast for a 0.3% gain. The control group, which flows directly into GDP estimates of consumption, declined by 0.1%, also below expectations for a 0.3% rise. In addition, the Fed started the easing cycle to support the labor market, which continues to soften. With the US central bank not wanting to see any more labor market cooling, we believe further Fed cuts remain on track.

Fed policymakers still view current policy as restrictive. While Powell said the strength of the US economy means the Fed is in no hurry to lower rates, he also noted the goal of bringing the policy rate to "the plausible range of neutral levels." This echoed recent comments by other Fed officials, who indicated that there is room for additional rate reductions. We don't expect the Fed to rush rate cuts, but we continue to believe that current US economic conditions do not warrant an actively restrictive monetary policy.

Central banks globally are also staying on the easing path. With the threat of tariffs weighing on sentiment and a fragile growth outlook, we think the European Central Bank might have to bring rates to neutral at a more rapid pace. Rate-cut expectations for the Swiss National Bank have also ramped up amid a benign inflation backdrop in Switzerland and lackluster growth in the Eurozone. For the Bank of England, while it should stick to a more gradual pace of easing following the rate cut earlier this month, the country's inflation is still expected to fall back to target over time. In Asia ex-Japan, policy interest rates should continue to be lowered to support domestic growth, especially as tariffs are imposed.

So we continue to recommend investors redeploy excess cash in a lower-rate environment, including investment grade bonds, diversified fixed income, and equity income strategies to enhance portfolio income.

Main contributors: Solita Marcelli, Mark Haefele, Daisy Tseng, Frederick Mellors, Brian Rose, Matthew Carter

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