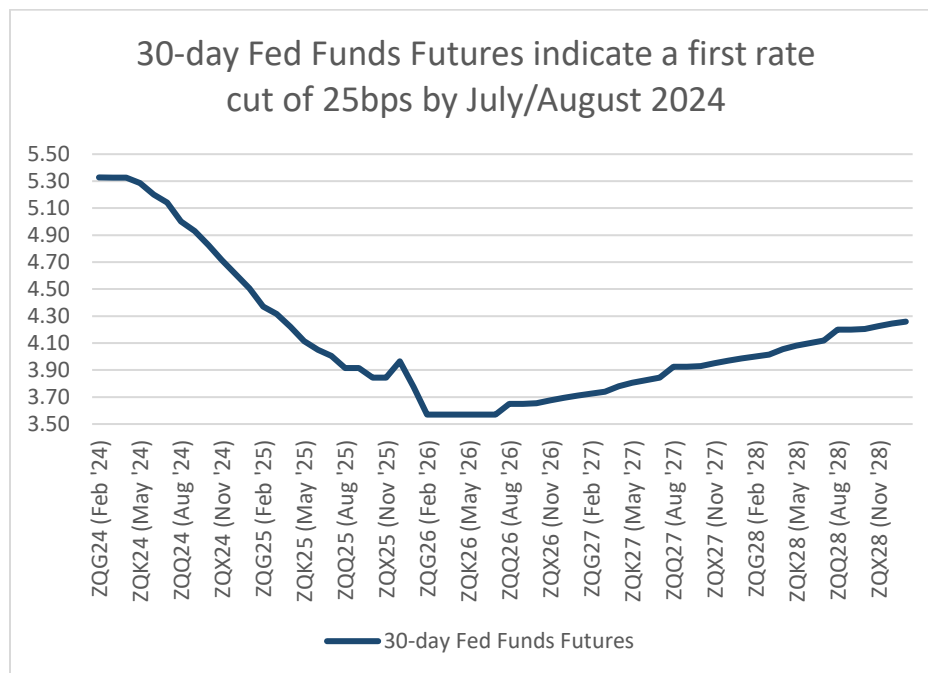


How the yield curve and interest rates compare in historical context

History shows us that Fed rate cuts won't be easy

When it comes to the Fed's hiking cycle and yield curve inversions, the current cycle looks very similar to rate hiking cycles in the past that led to significant market slowdowns or crashes. The number of weeks since the 10yr UST note is inverted vs. the Fed Funds rate has now approached over 67 weeks and it has been over 30 weeks since the last hike and no cut has occurred. The only period over the last 50 years that has longer duration of these two dynamics is the period ahead of the Global Financial Crisis with a total of over 81 weeks of a UST 10yr note vs. Fed Funds inversion and 58 weeks of last hike and first cut. If current fed funds futures are a fair guide, it is expected that the Fed cuts interest rates by 25bps around July/August for the first time, which would be the equivalent of 54 weeks between the last hike and first cut. However, the 10yr UST note vs. Fed Funds rate inversion is currently 110bps deep, and the first 100bps of cuts are only priced in by March 2025. This means, if the market is correct and the 10yr UST note remains at 4.24%, it would mark the longest 10yr UST note vs. Fed Funds inversion on record.



Source: Fred St. Louis

Fed Funds rate and yield curve inversion ahead of crises

Period	# of weeks UST 10yr - Fed Funds inversion	Weeks between last hike and first cut	Weeks between last hike and end of inversion
1973-74	99	1	26
1978-80	92	1	7
1982	17	1	16
1989	52	9	39
1998	29	12	16
2000-01	46	33	46
2006-09	81	58	77
2019	23	32	44
2020 Covid	4	-	-
Now	67 (so far)	30 (so far)	30 (so far)

Source: Fred St. Louis

How previous rate cuts came about: 2007

When comparing the most similar history of the current rate hiking cycle, the 2005-07 episode shares the most similarities. The current narrative of soft landing was not the case in 2007, however, as the Fed disappointed the market by cutting rates too slowly. The result was a liquidity crisis in August 2007 to which the Fed responded – however, not by cutting interest rates. The FOMC waited another full month to cut interest rates by 50bps on 18 September 2007. Following the first cut, a further 25bps cut occurred during the next meeting on 31 October 2007¹, a further 25bps cut on 11 December 2007², a 75bps cut on 22 January 2008³, 50bps cut on 30 January 2008⁴, and then emergency liquidity measures on 11 March 2008⁵ and another 75bps cut on 18 March 2008⁶. The sequence of these cuts is important as there is a

¹ <https://www.federalreserve.gov/newsevents/pressreleases/monetary20071031a.htm>

² <https://www.federalreserve.gov/newsevents/pressreleases/monetary20071211a.htm>

³ <https://www.federalreserve.gov/newsevents/pressreleases/monetary20080122b.htm>

⁴ <https://www.federalreserve.gov/newsevents/pressreleases/monetary20080130a.htm>

⁵ <https://www.federalreserve.gov/newsevents/pressreleases/monetary20080311a.htm>

⁶ <https://www.federalreserve.gov/newsevents/pressreleases/monetary20080318a.htm>

pattern, in which the Fed seems to avoid starting first interest rate cuts in Spring/early Summer (likely to avoid oil prices from heating up into the driving season), and with first panic setting in during January, after year-end.

FOMC statement regarding liquidity problem in August 2007

August 10, 2007

FOMC statement: The Federal Reserve is providing liquidity to facilitate the orderly functioning of financial markets

For immediate release

Share ➔

The Federal Reserve is providing liquidity to facilitate the orderly functioning of financial markets.

The Federal Reserve will provide reserves as necessary through open market operations to promote trading in the federal funds market at rates close to the Federal Open Market Committee's target rate of 5-1/4 percent. In current circumstances, depository institutions may experience unusual funding needs because of dislocations in money and credit markets. As always, the discount window is available as a source of funding.

August 17, 2007

FOMC statement

For immediate release

Share ➔

Financial market conditions have deteriorated, and tighter credit conditions and increased uncertainty have the potential to restrain economic growth going forward. In these circumstances, although recent data suggest that the economy has continued to expand at a moderate pace, the Federal Open Market Committee judges that the downside risks to growth have increased appreciably. The Committee is monitoring the situation and is prepared to act as needed to mitigate the adverse effects on the economy arising from the disruptions in financial markets.

Voting in favor of the policy announcement were: Ben S. Bernanke, Chairman; Timothy F. Geithner, Vice Chairman; Richard W. Fisher; Thomas M. Hoenig; Donald L. Kohn; Randall S. Kroszner; Frederic S. Mishkin; Michael H. Moskow; Eric Rosengren; and Kevin M. Warsh.

Source: Federal Reserve

FOMC statement on interest rate cut on 18 September 2007 meeting

September 18, 2007

FOMC statement

For immediate release

Share 

The Federal Open Market Committee decided today to lower its target for the federal funds rate 50 basis points to 4-3/4 percent.

Economic growth was moderate during the first half of the year, but the tightening of credit conditions has the potential to intensify the housing correction and to restrain economic growth more generally. Today's action is intended to help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in financial markets and to promote moderate growth over time.

Readings on core inflation have improved modestly this year. However, the Committee judges that some inflation risks remain, and it will continue to monitor inflation developments carefully.

Developments in financial markets since the Committee's last regular meeting have increased the uncertainty surrounding the economic outlook. The Committee will continue to assess the effects of these and other developments on economic prospects and will act as needed to foster price stability and sustainable economic growth.

Voting for the FOMC monetary policy action were: Ben S. Bernanke, Chairman; Timothy F. Geithner, Vice Chairman; Charles L. Evans; Thomas M. Hoenig; Donald L. Kohn; Randall S. Kroszner; Frederic S. Mishkin; William Poole; Eric Rosengren; and Kevin M. Warsh.

In a related action, the Board of Governors unanimously approved a 50-basis-point decrease in the discount rate to 5-1/4 percent. In taking this action, the Board approved the requests submitted by the Boards of Directors of the Federal Reserve Banks of Boston, New York, Cleveland, St. Louis, Minneapolis, Kansas City, and San Francisco.

Source: Federal Reserve

How previous rate cuts came about: 2001

The rate cut episode during 2001 was to some degree similar to 2007, as there were also large rate cuts during January. Back then, there was no rate cut accounted on 19 December 2000, but this was followed by an emergency 50bps rate cut on 3 January 2001, followed by another 50bps rate cut on 31 January 2001. This set in motion a long-running rate cut cycle, which ended at 1% in July 2003, at which point the market bottomed and stocks and oil began rising again.

FOMC statements on interest rate cut in January 2001

Federal Reserve Release

Press Release

Release Date: January 3, 2001



For immediate release

The Federal Open Market Committee decided today to lower its target for the federal funds rate by 50 basis points to 6 percent.

In a related action, the Board of Governors approved a 25-basis-point decrease in the discount rate to 5-3/4 percent, the level requested by seven Reserve Banks. The Board also indicated that it stands ready to approve a further reduction of 25 basis points in the discount rate to 5-1/2 percent on the requests of Federal Reserve Banks.

These actions were taken in light of further weakening of sales and production, and in the context of lower consumer confidence, tight conditions in some segments of financial markets, and high energy prices sapping household and business purchasing power. Moreover, inflation pressures remain contained. Nonetheless, to date there is little evidence to suggest that longer-term advances in technology and associated gains in productivity are abating.

The Committee continues to believe that, against the background of its long-run goals of price stability and sustainable economic growth and of the information currently available, the risks are weighted mainly toward conditions that may generate economic weakness in the foreseeable future.

In taking the discount rate action, the Federal Reserve Board approved requests submitted by the Boards of Directors of the Federal Reserve Banks of New York, Cleveland, Atlanta, St. Louis, Kansas City, Dallas and San Francisco.



Press Release

Release Date: January 31, 2001

For immediate release

The Federal Open Market Committee at its meeting today decided to lower its target for the federal funds rate by 50 basis points to 5-1/2 percent. In a related action, the Board of Governors approved a 50 basis point reduction in the discount rate to 5 percent.

Consumer and business confidence has eroded further, exacerbated by rising energy costs that continue to drain consumer purchasing power and press on business profit margins. Partly as a consequence, retail sales and business spending on capital equipment have weakened appreciably. In response, manufacturing production has been cut back sharply, with new technologies appearing to have accelerated the response of production and demand to potential excesses in the stock of inventories and capital equipment.

Taken together, and with inflation contained, these circumstances have called for a rapid and forceful response of monetary policy. The longer-term advances in technology and accompanying gains in productivity, however, exhibit few signs of abating and these gains, along with the lower interest rates, should support growth of the economy over time.

Nonetheless, the Committee continues to believe that against the background of its long-run goals of price stability and sustainable economic growth and of the information currently available, the risks are weighted mainly toward conditions that may generate economic weakness in the foreseeable future.

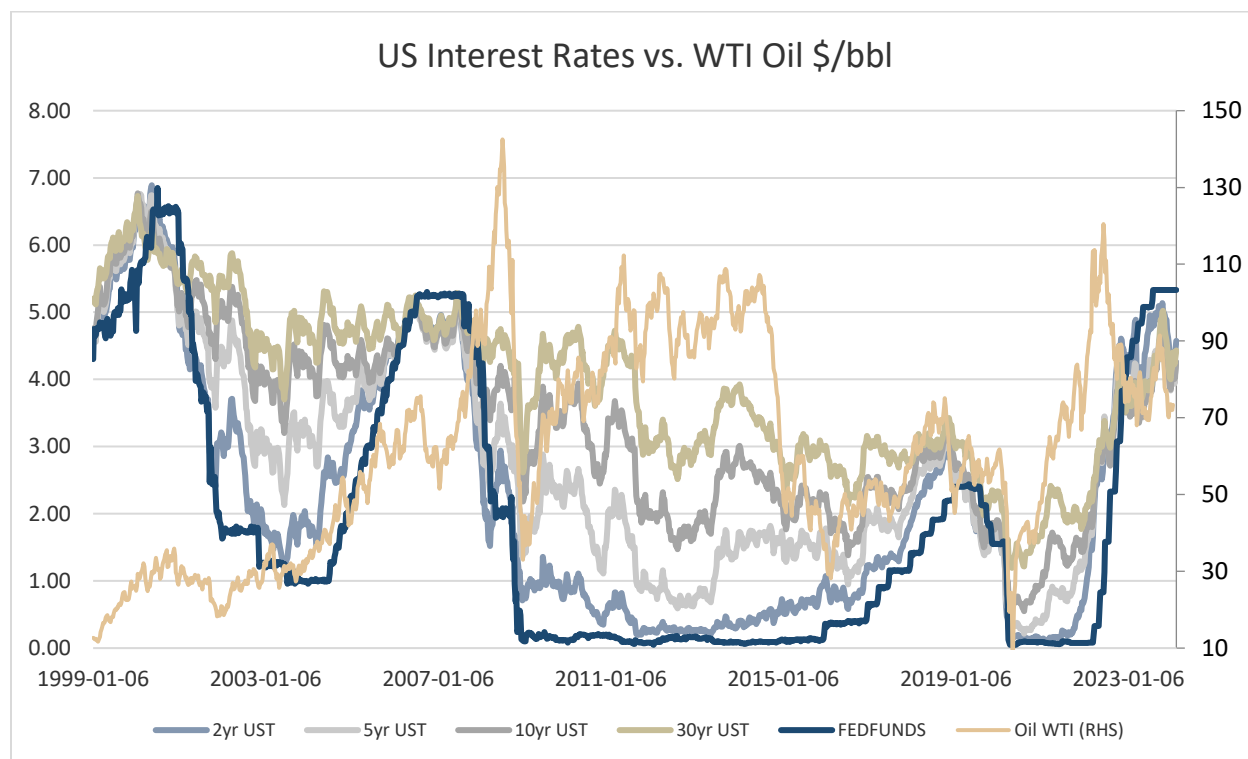
In taking the discount rate action, the Federal Reserve Board approved requests submitted by the Boards of Directors of the Federal Reserve Banks of New York, Philadelphia, Cleveland, Atlanta, Chicago, St. Louis, Minneapolis, Dallas and San Francisco.

Source: Federal Reserve

Interest rate reduction cycle: In Conclusion

History shows us that the current rate hiking cycle is at its end. However, a soft landing has historically never occurred, and cutting interest rates, especially when left high for too long, has often been led by a general downturn in markets. Oil, on the other hand, showed strength in the beginning of the 2007/08 cutting cycle. In fact, if oil prices would begin to strengthen into the summer, it would very much look like 2007 again, with higher yields, higher oil prices, and the Fed unable to lower interest rates. What is quite different this time though, we already are in a recession in Europe, and if it wasn't for all the military and fiscal spending, we would be in a recession in the US, too. A look at natural gas prices also suggests that inflation is very well under control. In the UK, the average energy bill will fall by 12% in April 2024, and the National Institute of Economic and Social Research predicts that UK inflation will drop below 2% as a result

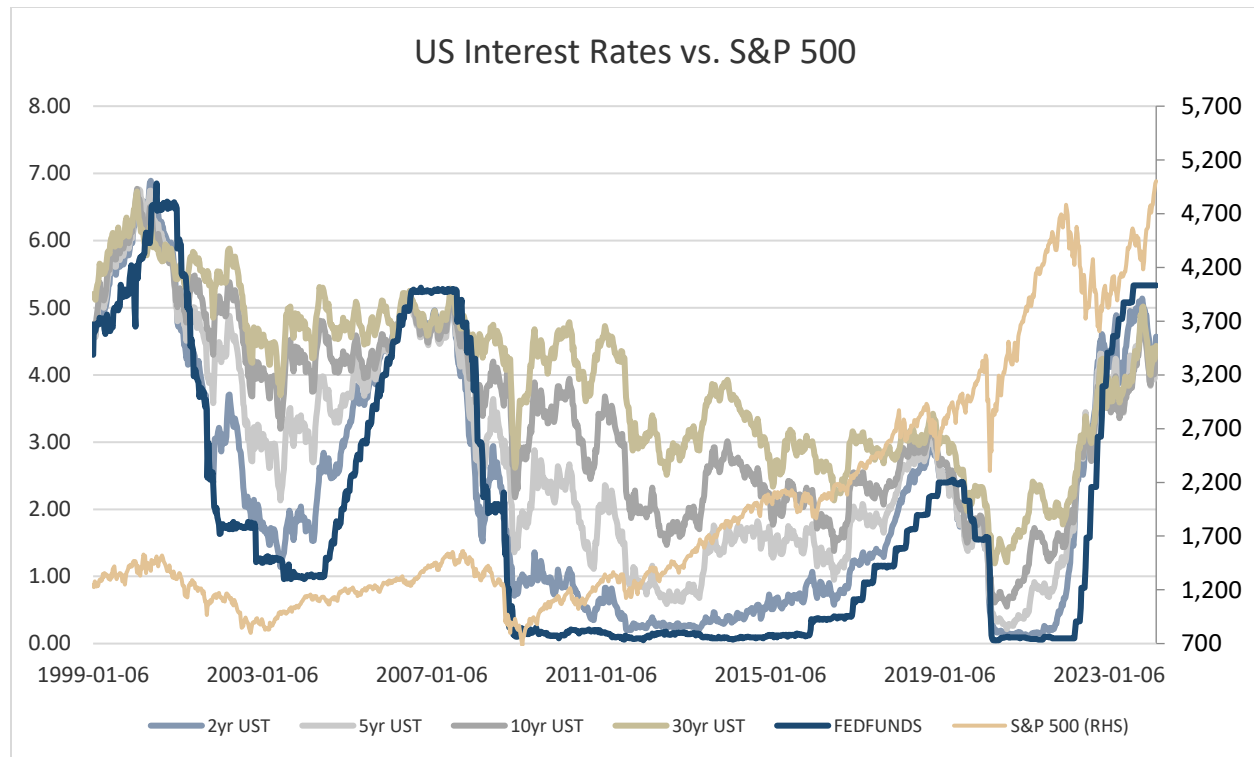
of it⁷. This could enable the BOE to cut rates quickly, especially given the current natural gas futures curve, which indicates further falls for the months ahead⁸. The risk/return for owning long duration are hence extremely attractive now.



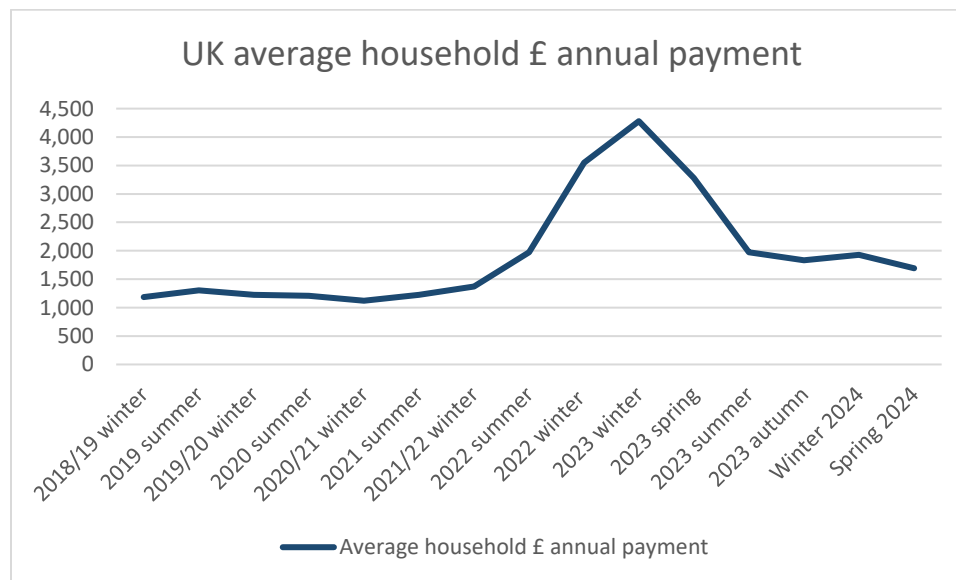
Source: FRED St. Louis

⁷ [Inflation Expected to Fall Below Two Per Cent by April - NIESR](#)

⁸ https://www.barchart.com/futures/quotes/NF*0/futures-prices



Source: FRED St. Louis



Source: Ofgem



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