

# What do Fed rate cuts mean for investors?

## UBS House View Briefcase

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### Key message

The Federal Reserve resumed its rate-cutting cycle in September and signaled more easing ahead. A cooling US labor market gives room for the Fed to cut rates further, despite lingering inflation concerns. We expect another 75bps of rate cuts between now and the first quarter of 2026, and with policy rates set to fall, we advise investors to put cash to work.

### House view

#### 01 **The Fed resumed its rate-cutting cycle in September.**

- The Fed cut policy rates by 25 basis points in September, its first reduction since 2024.
- Policymakers' median projection for the federal funds rate (the dot plot) now indicates two additional cuts are expected this year.
- The FOMC's latest economic projections show inflation near its target in 2027.

#### 02 **A softening labor market gives the Fed scope to continue easing.**

- The FOMC's September statement said the committee "judges that downside risks to employment have risen."
- We believe concerns about a weakening labor market are likely to outweigh those about lingering inflation in the Fed's decision-making.
- Given the Fed's dual mandate, we expect rates to come down by a further 75 basis points by the end of the first quarter of 2026.

#### 03 **With policy rates set to fall further, investors should put cash to work now.**

- We recommend that investors phase excess liquidity into diversified portfolios.
- To achieve alternative sources of portfolio income to cash, we see medium-duration quality bonds and equity income strategies as appealing.
- We also expect lower interest rates, robust corporate earnings, and AI tailwinds to support further gains for equity markets over the coming year.

### New this week

Federal Reserve Chair Jerome Powell laid the ground for an October rate cut in remarks on 14 October, and surprised investors with a longer discussion about the US central bank's quantitative tightening (QT) policy, which may be coming to an end sooner than widely thought. Market participants interpreted these remarks as dovish, with equities rising intra-session on the headlines, both 10- and 30-year Treasury yields dipping to multi-month lows, and gold braking above USD 4,200/oz.

### One liner

With the Fed likely to cut rates further, we recommend putting excess cash to work.

### Did you know?

- Soft landing rate cuts have historically been positive for stocks, and the Fed's shift from restrictive to more neutral policy should help extend the bull market.
- In a downside scenario, if labor market weakness proves to be more severe or durable, we believe the Fed could cut rates by 200-300bps by mid-2026.
- Cash tends to underperform other assets over time: Stocks have outperformed cash in 86% of all 10-year periods and 100% of all 20-year periods since 1926, with cumulative returns more than 200 times higher than cash over the long term.

### Investment view

We believe the resumption of the Fed's rate-cutting cycle increases the imperative for investors to put cash to work. We recommend phasing excess liquidity into diversified portfolios. We also continue to like quality bonds, which can offer a more durable source of income. Investors underallocated to equities should consider adding to stocks in CIO's preferred areas, including AI, Power and resources, and Longevity.

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