# What does Fed policy mean for investors?

## UBS House View Briefcase

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## Key message

The timing of the next rate cut may be delayed by stronger growth data and early signs of stabilization in the labor market, but the likelihood of further easing increases the importance of putting excess cash to work for investors.

### 01 The Fed is likely to hold rates steady until June.

- The Fed held rates steady in January after three consecutive reductions last year, upgraded its growth assessment and highlighted signs of stabilization in the labor market.
- January's labor report was stronger than expected, with the unemployment rate edging lower to 4.3%.
- Many FOMC participants remain uncomfortable looking through tariff-related inflation pressures in the near term, making it difficult to form a consensus on further rate cuts.

### 02 But we believe the Fed has scope to ease by another 50 basis points this year.

- The Fed's guidance signals a strong inclination to continue lowering rates toward 3%.
- By mid-2026, the path for rate cuts should become easier as 2H growth slows and goods inflation eases. We expect the next rate cut in June, followed by a second in September, bringing the policy rate range to 3.00-3.25%.
- A more dovish personnel profile at the Fed Board later this year should support rate cuts.

### 03 Lower interest rates strengthen the case for investors to put cash to work.

- Investors should consider phasing 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 and robust corporate earnings to support further gains for equity markets.

## New this week

US CPI rose 0.2% m/m in January, the smallest gain since July and restrained by lower energy costs. Core CPI, which excludes food and energy, advanced 0.3% from a month earlier, in line with market expectations.

## One liner

For investors, Fed rate cuts increase the importance of putting excess cash to work.

## Did you know?

- Former Governor Warsh's recent comments suggest a preference for lower rate policy. He has said he favors looking through tariff inflation and thinks current productivity trends will be disinflationary. These comments are consistent with our view that the easing cycle is intact.
- Moreover, the seven permanent FOMC board voters, both current and prospective, tend to be moderately more dovish than the median forecast and generally view neutral as closer to 3% or below.
- 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.

## Investment view

Lower interest rates reduce potential returns on cash. We therefore recommend that investors consider phasing excess liquidity into diversified portfolios. We also 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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