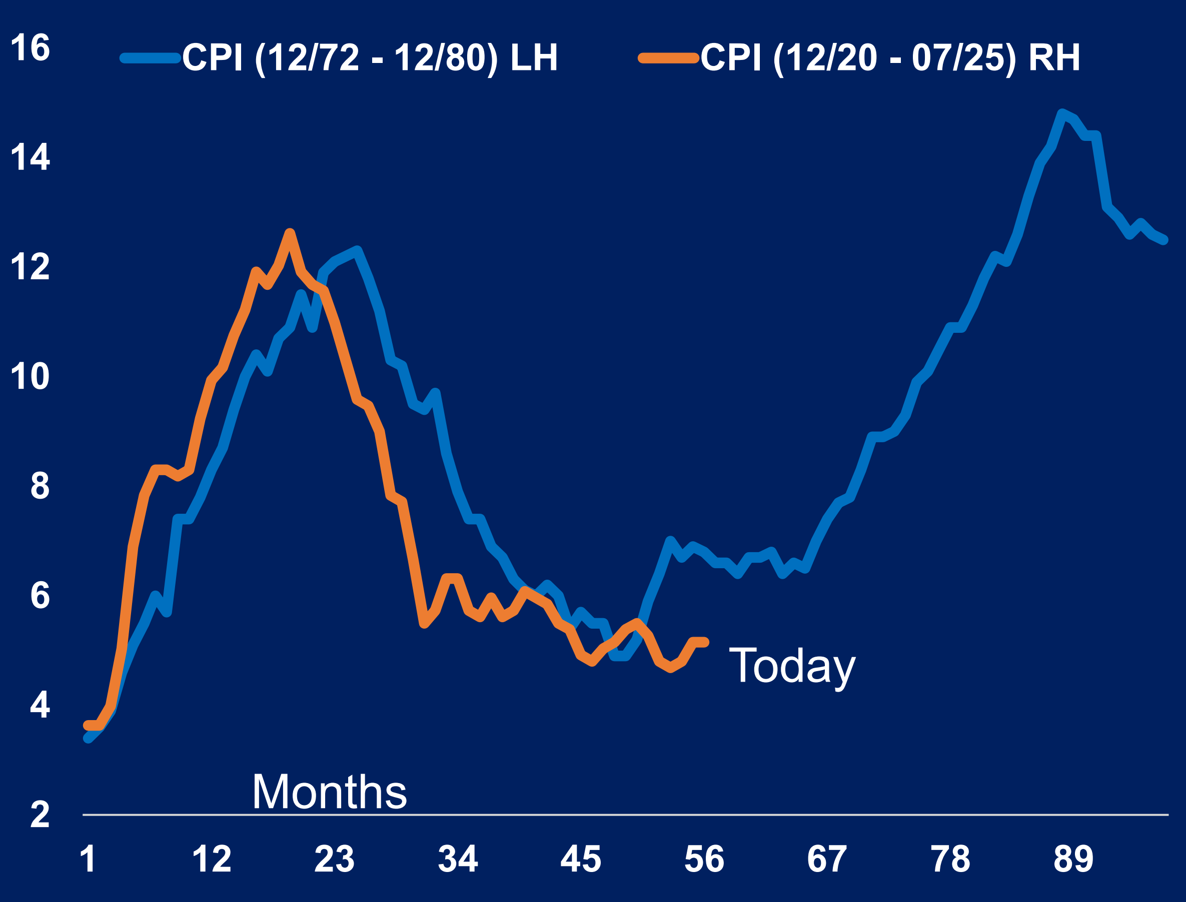
Rubrics Fixed Income Macro View

America’s Next Nixon/Burns

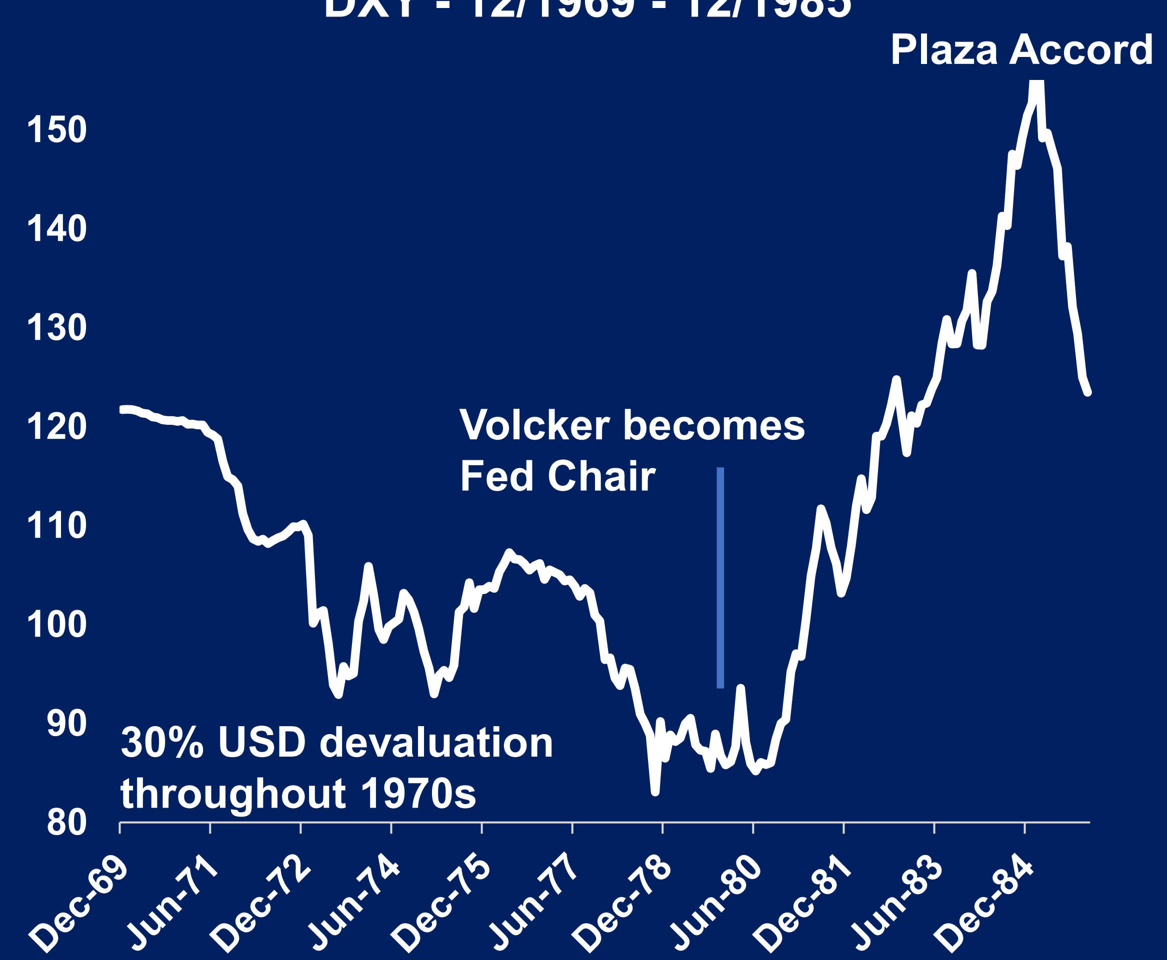
A sitting President leaning on a compliant Fed Chair is not unprecedented in US history. One of the most infamous examples involved Nixon pressuring Fed Chair Arthur Burns to cut interest rates ahead of the 1972 election. It would be fair to say that did not end well. Though today’s environment does not exactly mirror that of the 1970s - Powell is yet to ‘bend the knee’ to Trump – the growing influence of Treasury Secretary Scott Bessent and his willingness to openly call for lower rates has distinct echoes. Indeed, it was he who mooted the idea of nominating a ‘Shadow Fed Chair’ ahead of Powell’s cessation next year. Far from acting as a counterweight to Trump’s impetuousness – Bessent appears fully bought in.

CPI Inflation (1970s vs 2020s)



Source: Bloomberg as at 31/07/25

DXY - 12/1969 - 12/1985



Source: Bloomberg as at 31/07/25

The cost of abandoning a credible commitment to price stability is immense. If markets begin to believe that inflation control is subordinate to political expediency, long-term borrowing costs could surge. This would ripple across global markets risking a confidence shock that could require a Volcker-style intervention — something that would not spare even the wealthiest Americans.

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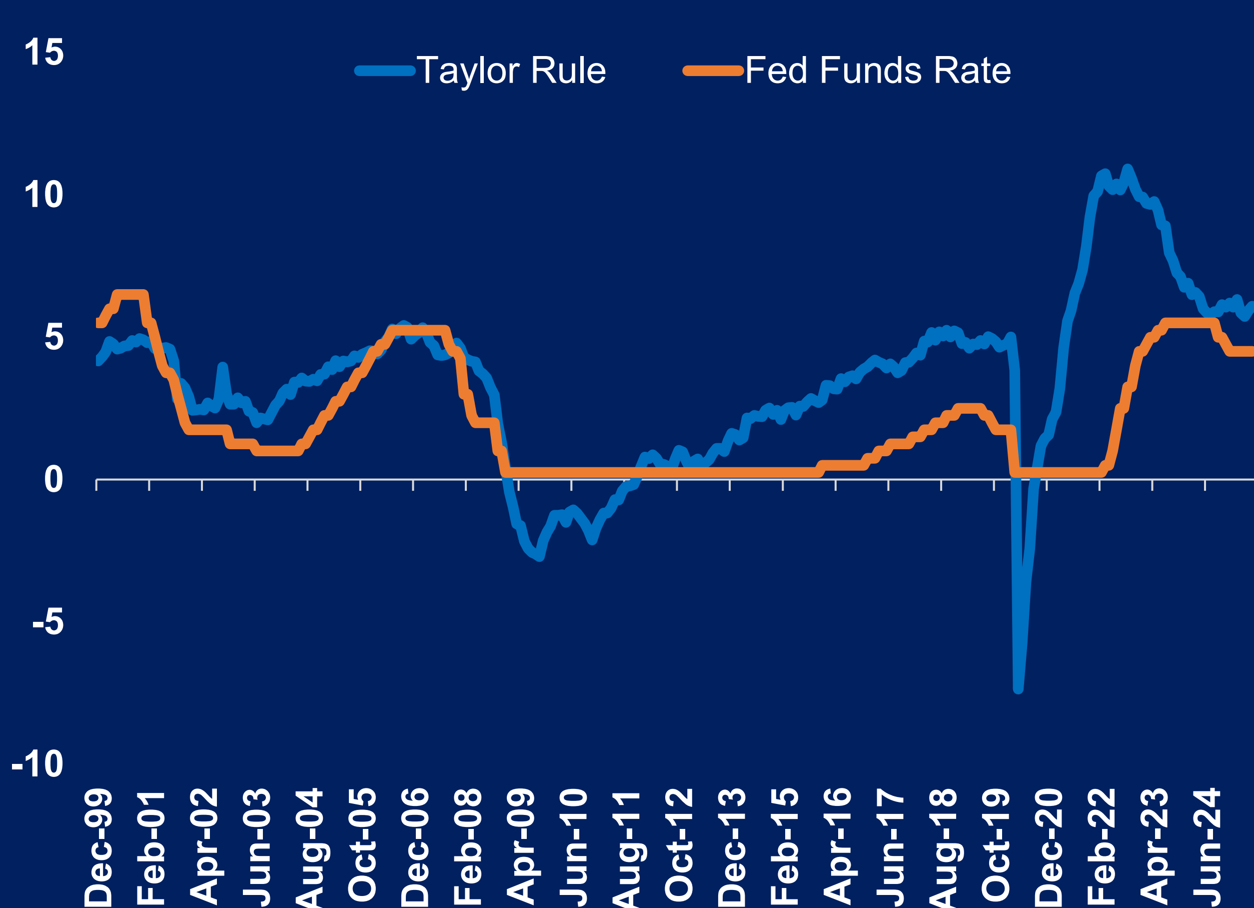
Is the ‘Shadow Fed’ Right to Call for Rate Cuts?

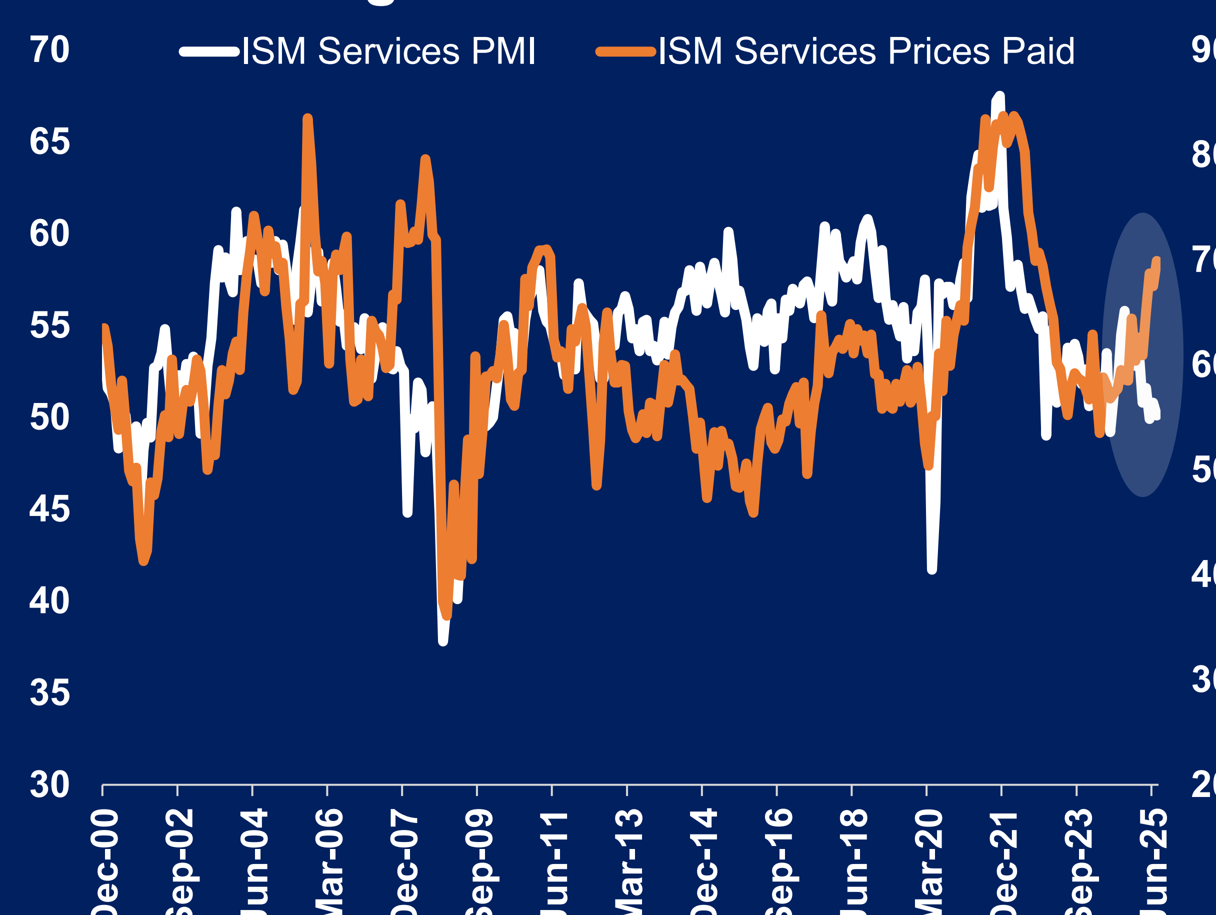
Bessent’s recent claim that ‘by any model’ the Fed Funds rate should be 150 to 175 bps lower doesn’t pass the eye test. Indeed, one of the best-known interest rate models – the Taylor Rule - suggests the Funds rate should be approximately 150 bps higher. The discernible pickup in a broad range of inflationary data points throws additional water on the suggestion that getting rates down fast is a ‘no brainer’. Notwithstanding the Trump’s histrionics, cutting into an inflationary environment might well do more harm than good.

Taylor Rule vs Fed Funds



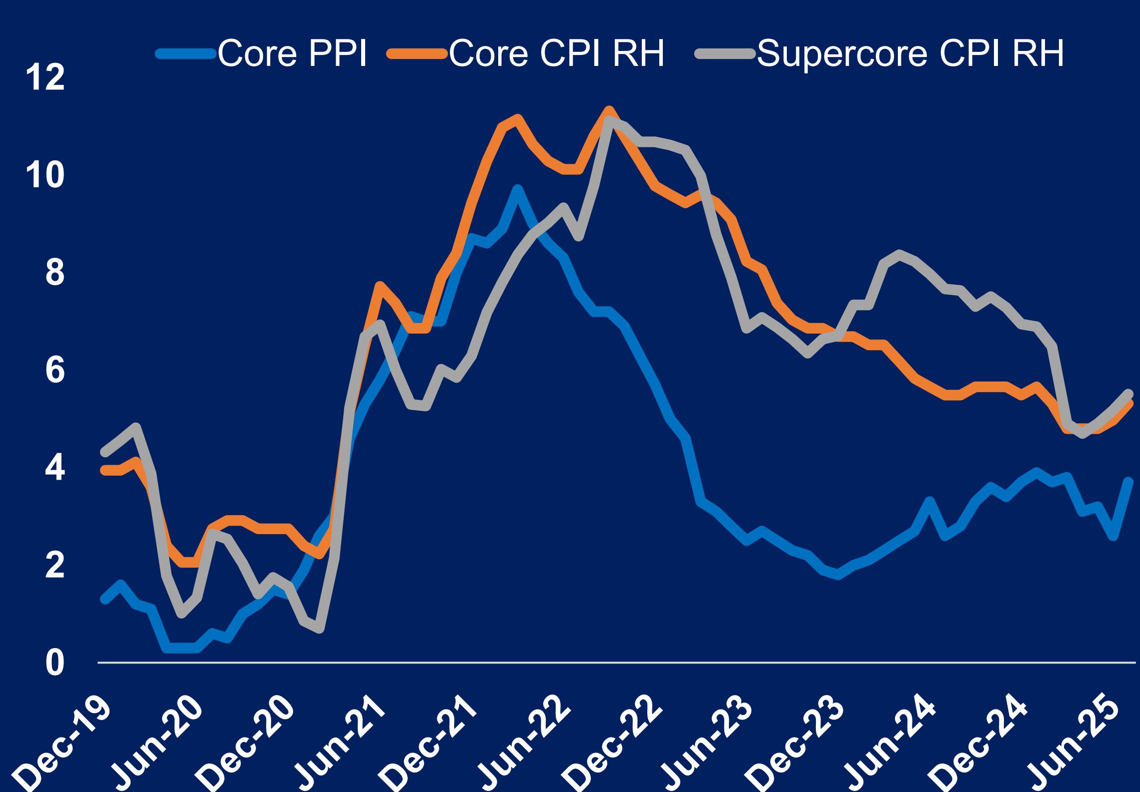
Source: Bloomberg as at 31/07/25

Stagflation - Services PMI



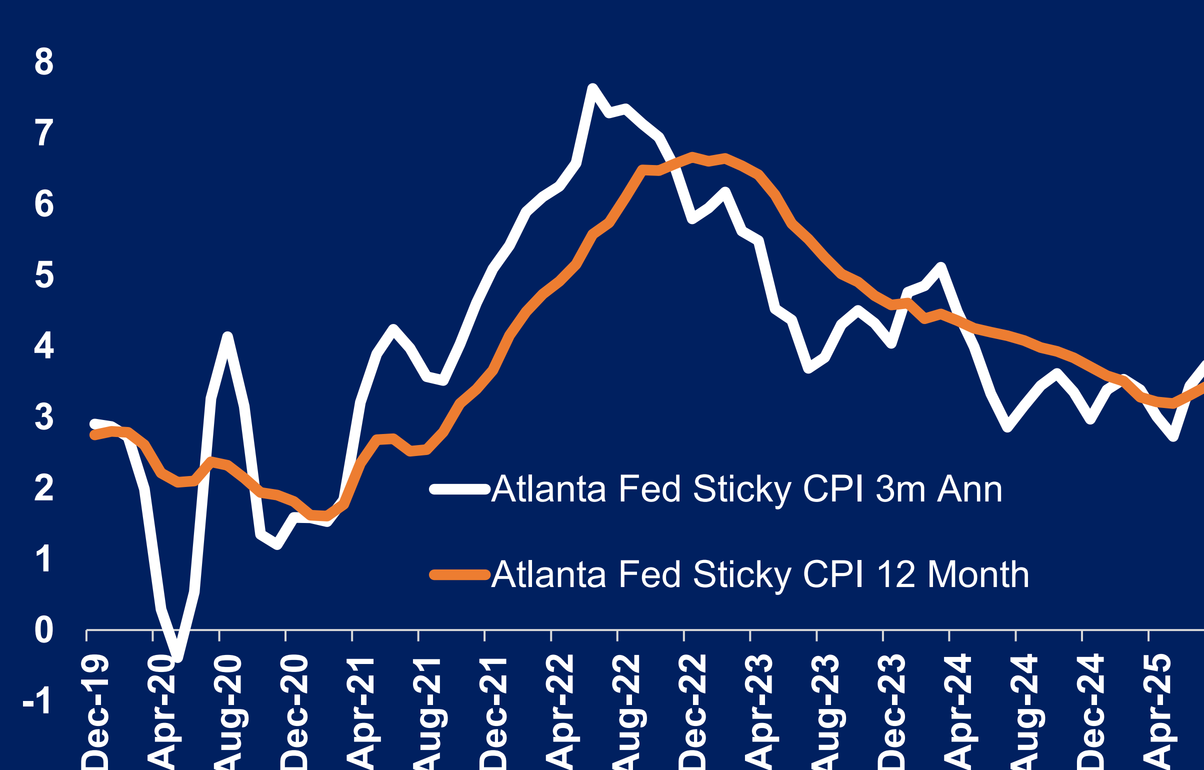
Source: Bloomberg as at 31/07/25

Core PPI vs CPI



Source: Bloomberg as at 31/07/25

Atlanta Fed Sticky CPI



Source: Bloomberg as at 31/07/25

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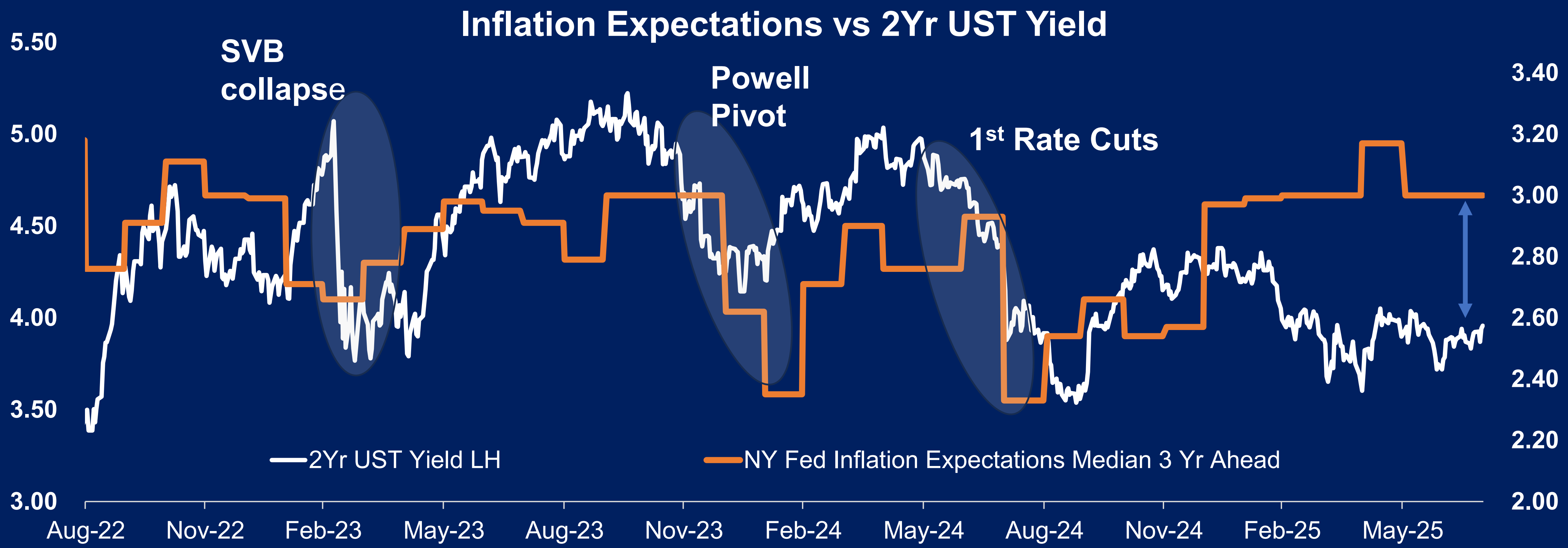
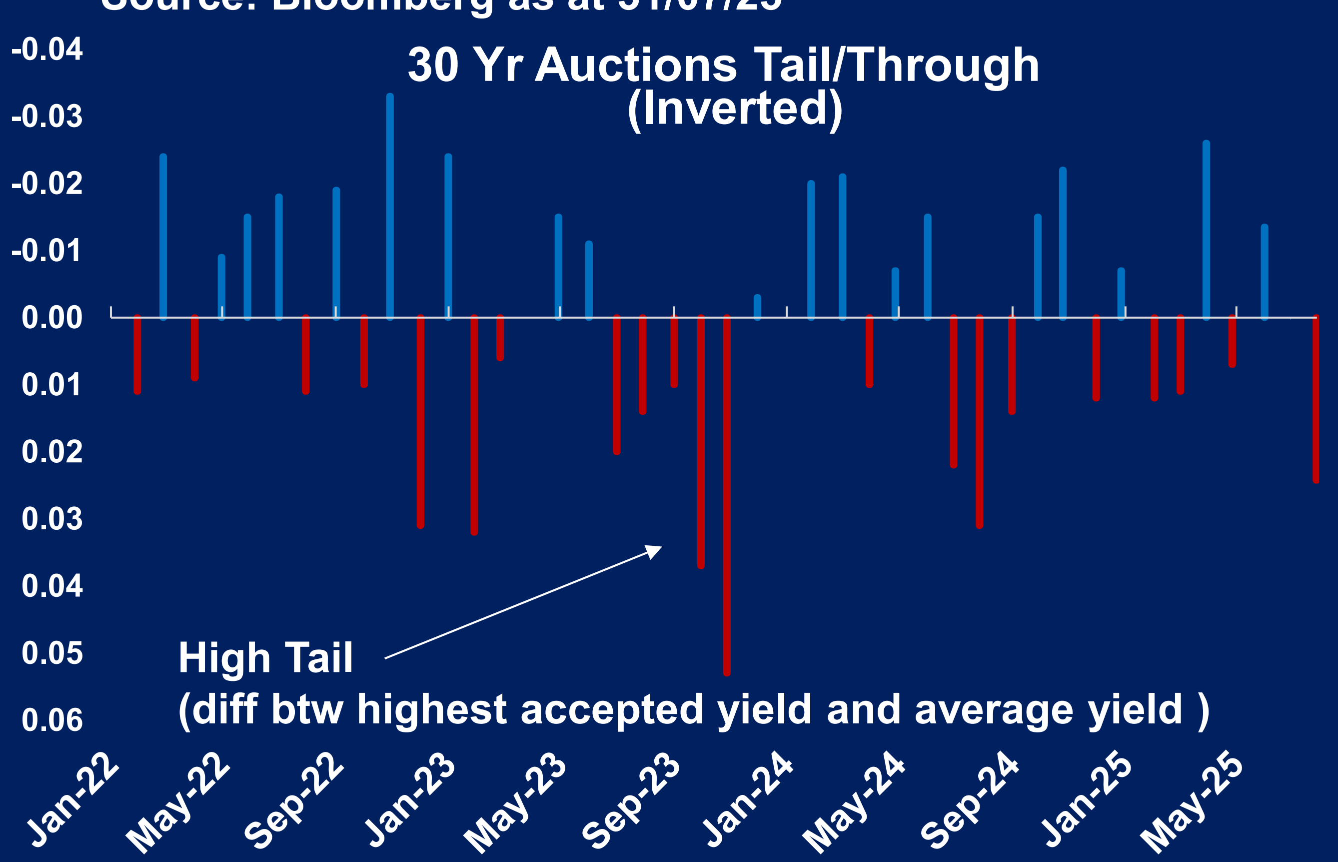
The Problem with Cutting Now – Vigilantes

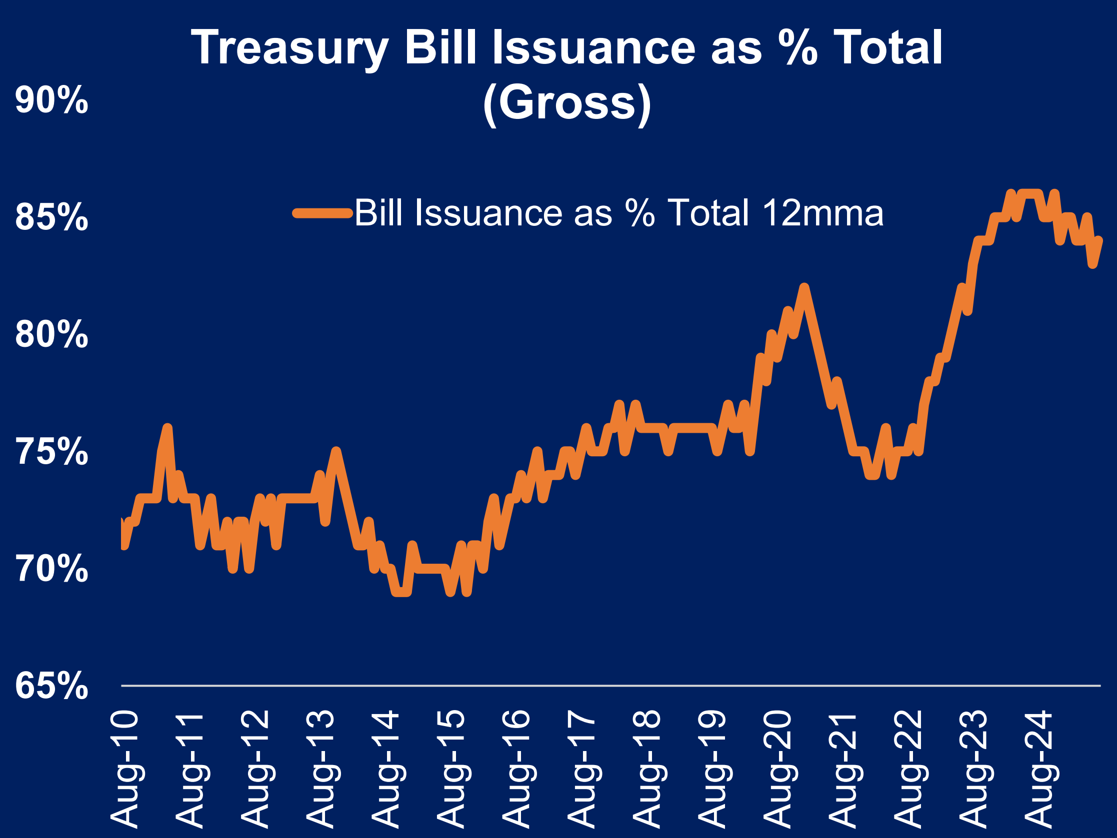
There is a strong sense of déjà vu to the idea of the Fed re-initiating their cutting cycle. Post 2022 there have been several 'false dawns' involving multiple rate cuts being priced into the curve, only to be priced out almost as swiftly. What makes today's environment more challenging is the fact that inflation expectations have begun detaching themselves from interest rates – amplifying the risk of a Fed mistake if they act too aggressively. This, it should be remembered, is against a backdrop of record Bill issuance designed to take pressure off the long end of the curve which has struggled in recent auctions. The lesson from history is clear – do not ignore the bond market.



Source: Bloomberg as at 31/07/25



Source: Bloomberg as at 31/07/25



Source: Bloomberg as at 31/07/25

Rubrics Fixed Income Macro View

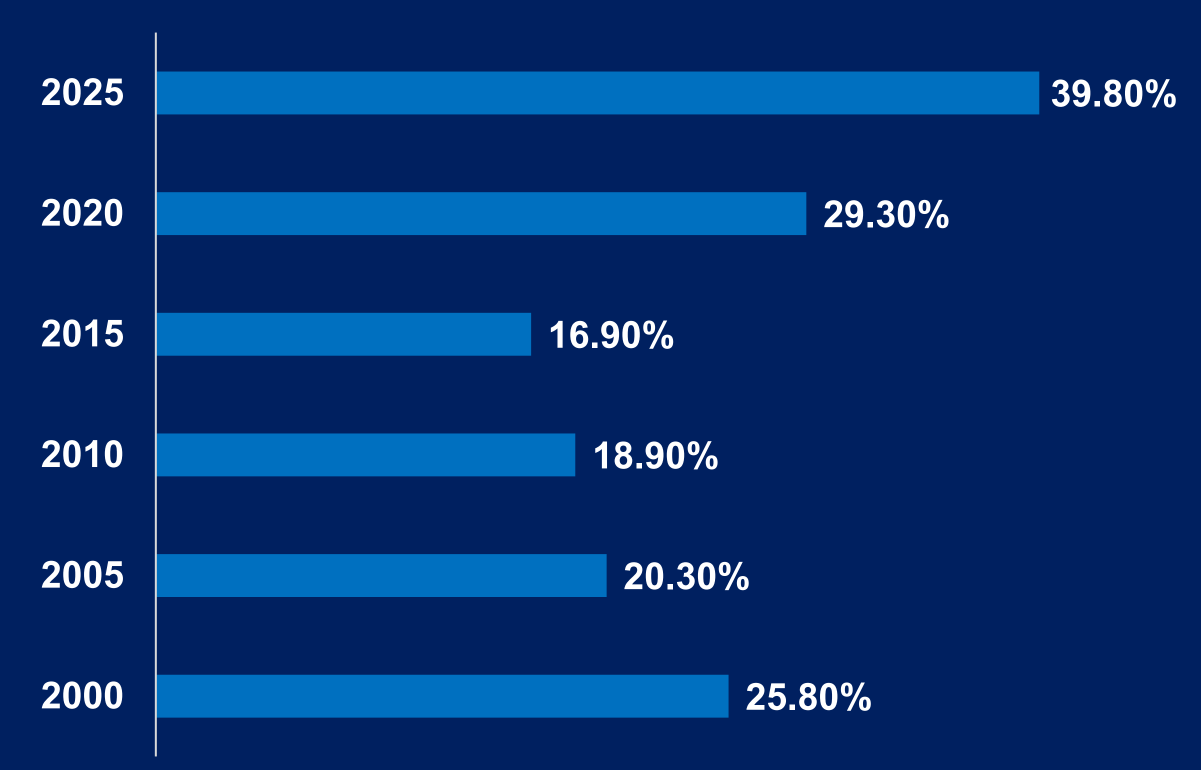
The Problem with Cutting Now – Asset Bubbles

By many metrics market valuations appear increasingly stretched with concentration at unparalleled levels. Considering this, the reignition of an aggressive cutting cycle risks fuelling a further melt-up in financial assets, (the bigger the bubble……) while the return of SPACs highlights the risks around speculative investment. The fact that credit spreads have also priced in an extremely benign economic outcome – despite signs of growing distress in private markets – is yet further evidence of the widespread complacency in financial markets.

S&P 500 Today vs Dot Com

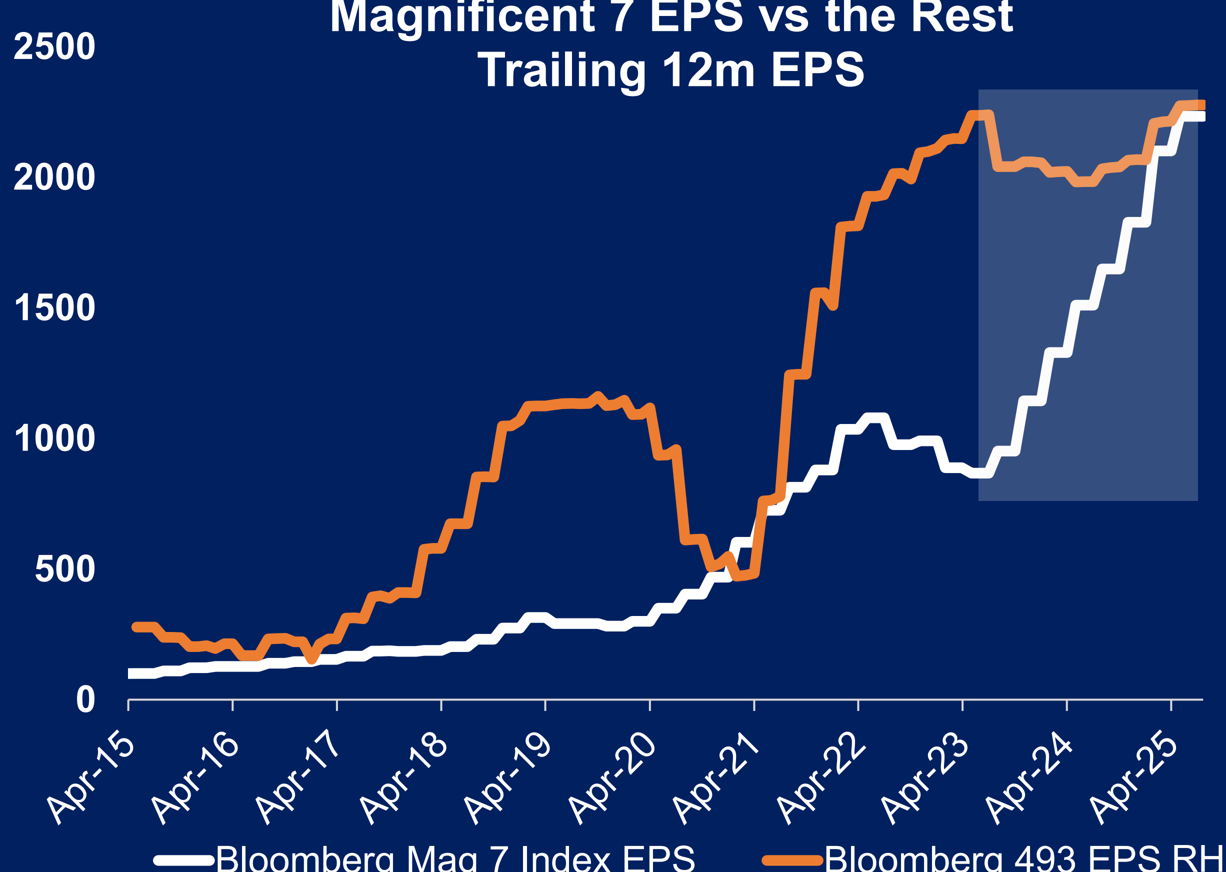
Source: Bloomberg as at 19/08/25

Share of Top 10 Companies in S&P 500



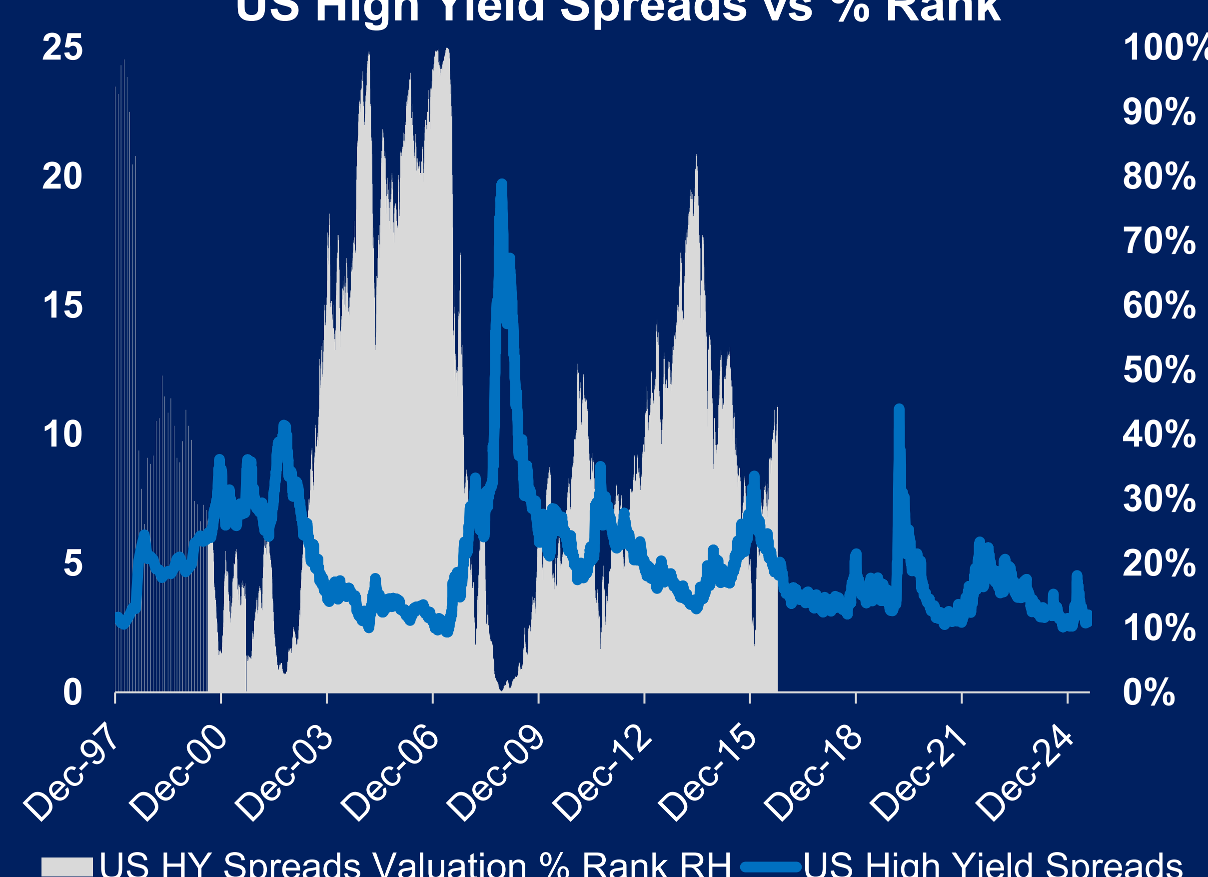
Source: Bloomberg as at 19/08/25

Magnificent 7 EPS vs the Rest Trailing 12m EPS



Source: Bloomberg as at 19/08/25

US High Yield Spreads vs % Rank



Source: Bloomberg as at 19/08/25

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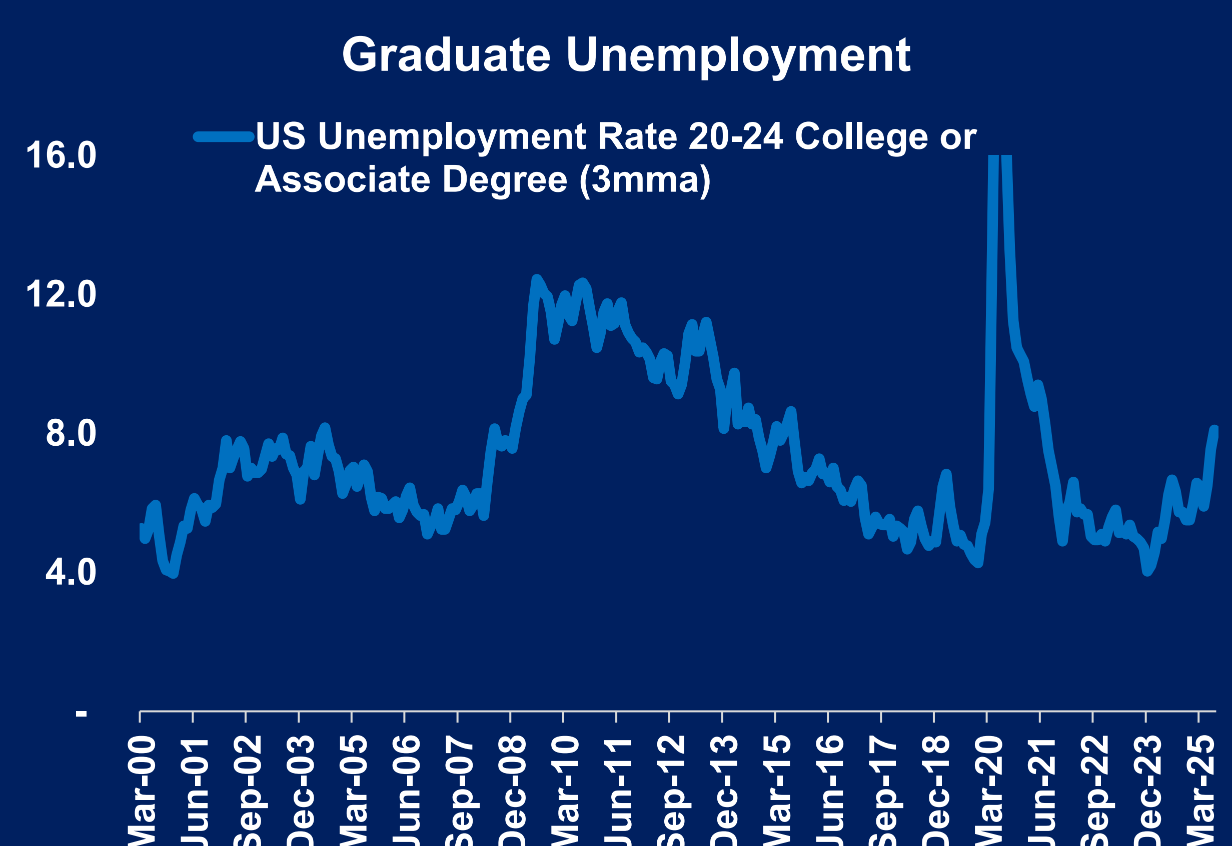
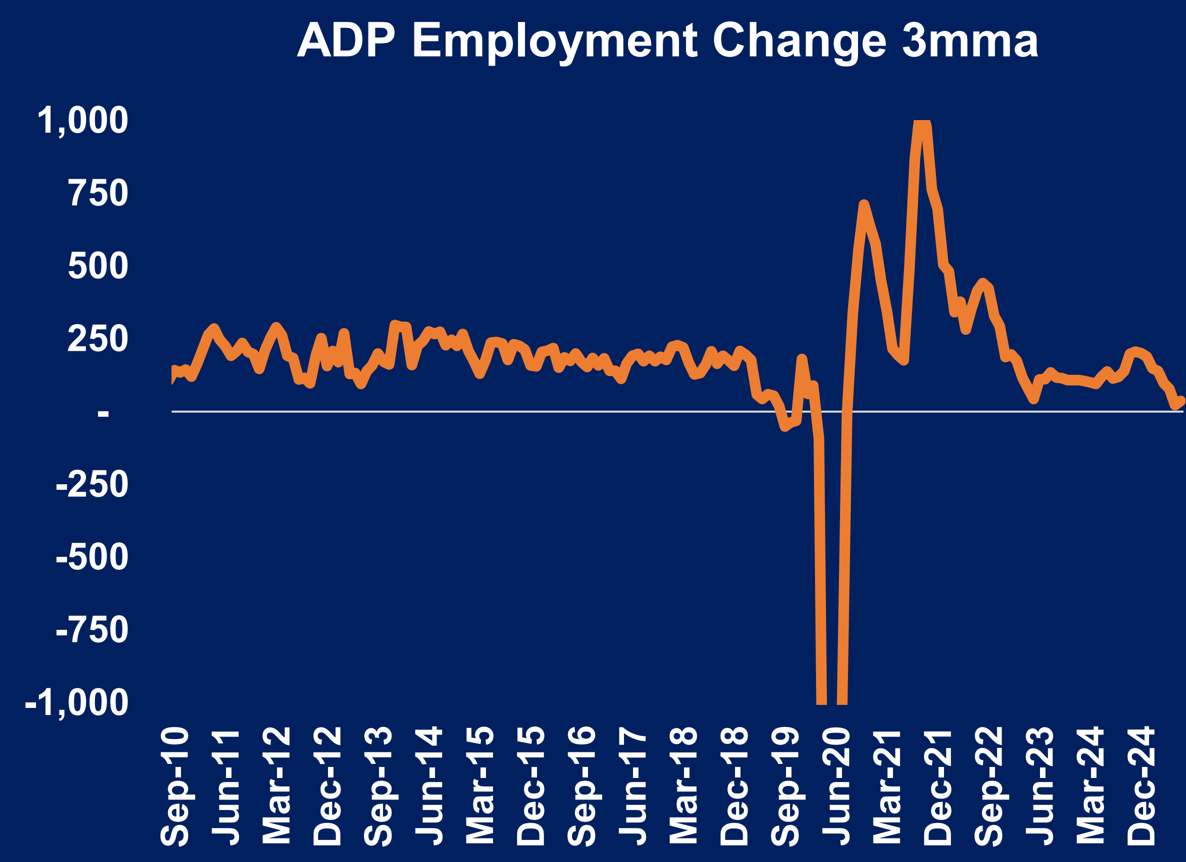
Long Term Plan – Get Real Rates Down

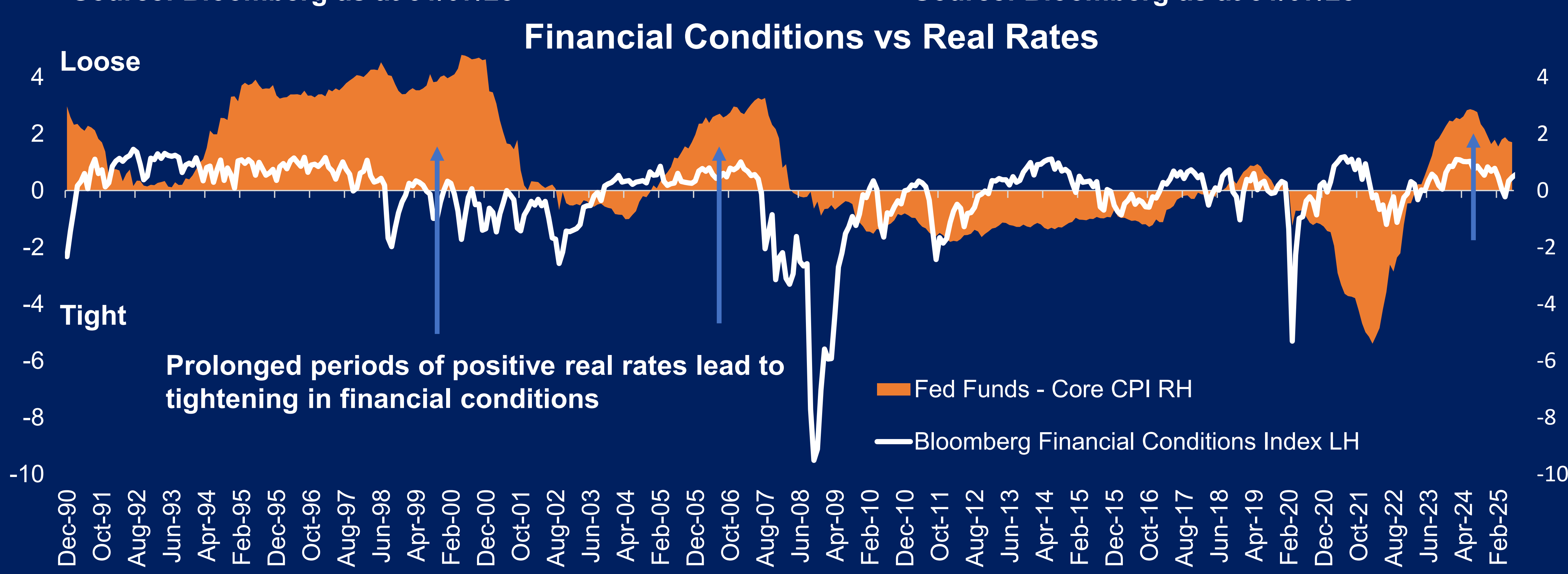
Notwithstanding the logic for caution on cutting rates in the short term, there are several signs the economy is slowing. Most tellingly both the jobs market and the consumer are showing signs of a slowdown. In addition, and arguably of greater concern to the Trump administration, the \$1.6trln of new debt issuance required between now and year end[1] (a significant increase on April estimates) could certainly do with lower interest rates. Longer term, the only way to sustain current levels of debt is to get real rates as low as is feasibly possible (preferably via lowering interest rates not financial repression). The longer real rates stay positive – the greater the likelihood of a major economic contraction.



Source: Bloomberg as at 31/07/25



Source: Bloomberg as at 31/07/25



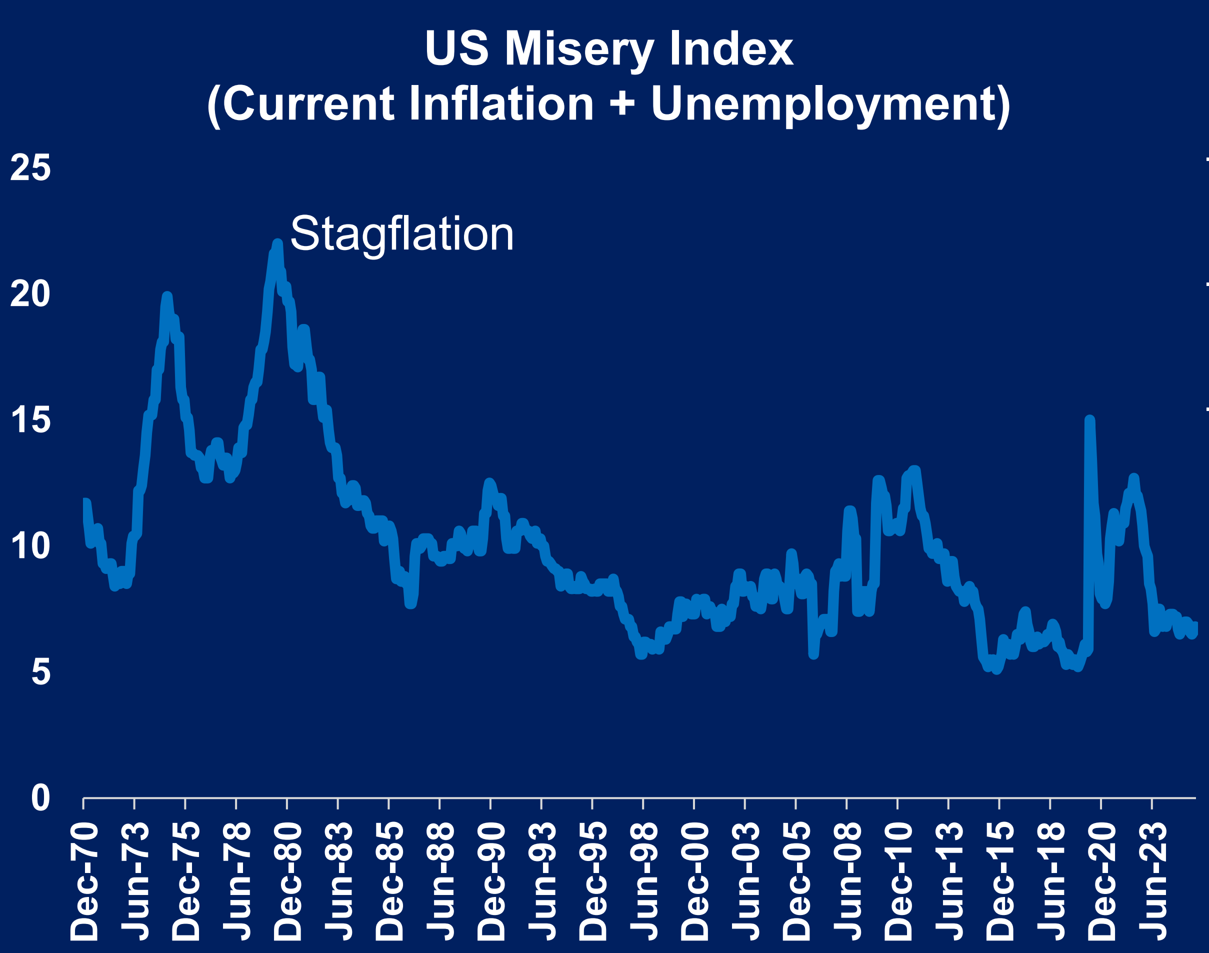
Source: Bloomberg as at 31/07/25

1. Treasury Announces Marketable Borrowing Estimates | U.S. Department of the Treasury

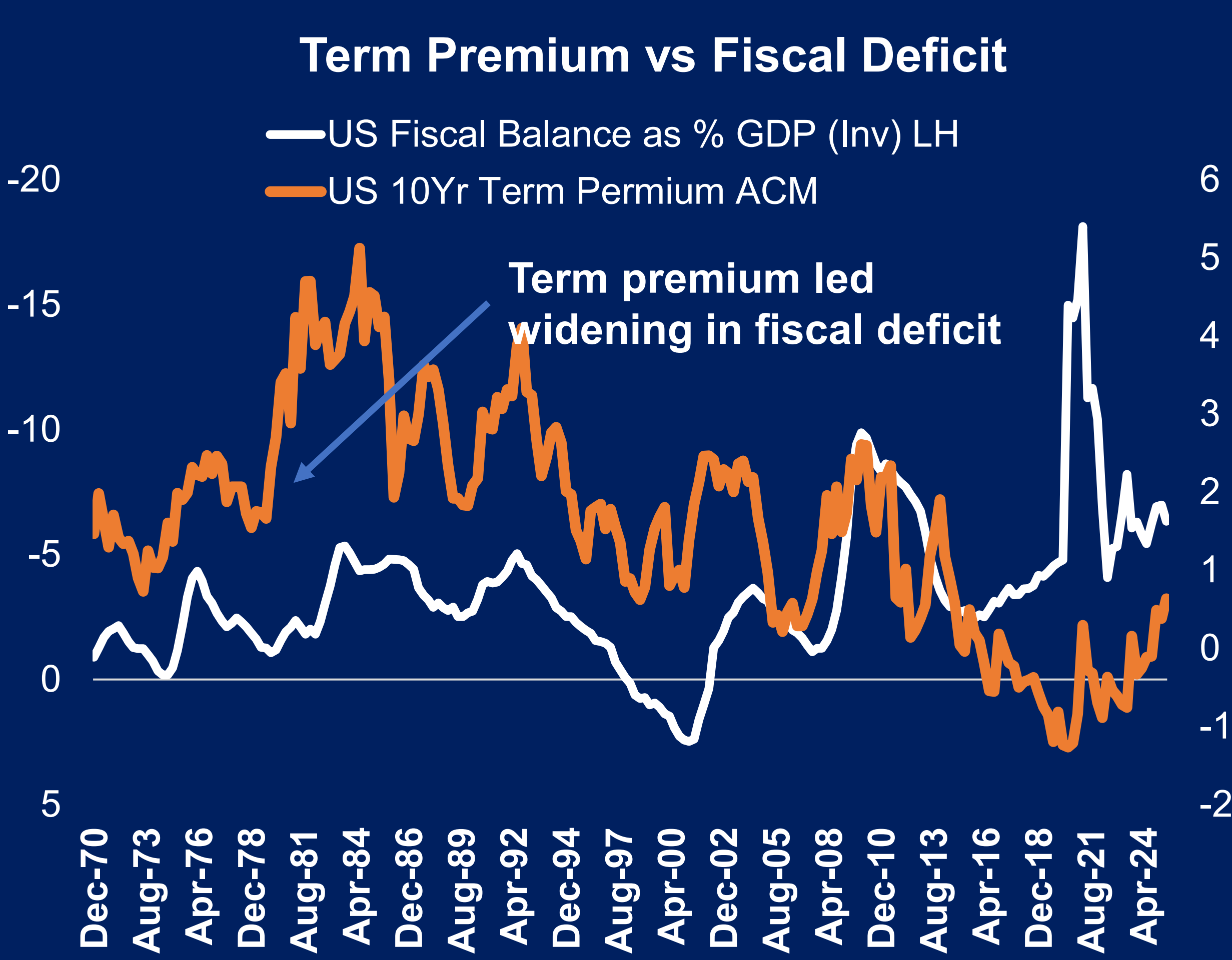
Rubrics Fixed Income Macro View

What Needs to Happen

Scott Bessent noted at the start of his tenure as Treasury Secretary that the important variable for the administration to watch was the 10-year Treasury yield, not the Fed Funds rate. If this were truly the focus of the administration, they would support the decision to hold off cutting rates for now which could ultimately stop the (self-induced) inflationary problems from escalating. Might this risk bringing forward a recession? Possibly, but it might also allow scope for further cuts down the line. Nobody, least of all Trump, should want a re-run of the 1970s, particularly with deficits at current levels.



Source: Bloomberg as at 31/07/25



Source: Bloomberg as at 30/06/25

However Trump is Trump and he is surrounded by a cabinet with a similarly short-term mindset. If he can get his way, he will. In the short term though, this is far from a fait accompli and the power at the Fed does not (yet) reside in the hands of the Administration. A lot can happen between now and the time Powell steps down – the economy may be in a different place by May 2026. Perhaps letting nature take its course might just be the best solution of all.

Important Information