

## Fed Stands Pat

- Fed hold rates steady at 5.25%-5.50%
- Fed acknowledge lack of progress in disinflation
- Fed said rate hikes remain “unlikely” despite lack of inflation progress
- Rate cuts remain on the cards for 2024, but inflation progress and labor market softness is required

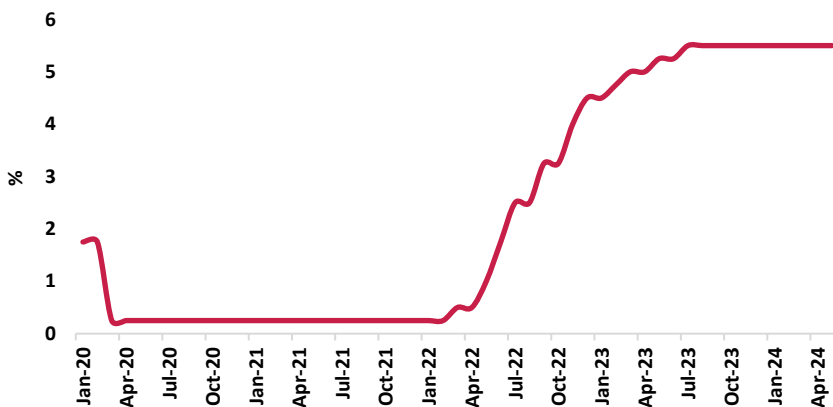
The Federal Reserve held interest rates steady for a fifth straight meeting with the FOMC signalled it is in no rush to reduce rates. The decision to leave the target range for the benchmark federal funds rate unchanged at a 22-year-high of 5.25% to 5.5% was unanimous given inflation continues to run too hot for comfort, consumers are still spending strongly and the economy added more than 800,000 jobs in the first three months of the year. The federal funds rate has been at that level since July 2023, when the Fed last hiked and took the range to its highest level in more than two decades.

In the accompanying statement they continue to acknowledge that “inflation has eased over the past year but remains elevated”, but they have added the caveat that “in recent months, there has been a lack of further progress toward the Committee’s 2 percent inflation objective”, reiterating language it had used after the January and March meetings. The statement also altered its characterization of its progress toward its dual mandate of stable prices and full employment. The new language hedges a bit, whereby risks to achieving their employment and inflation goals “have moved toward better balance over the past year”. Previously they suggested the risks were “moving into better balance”. Beyond that, the statement was little changed, with economic growth characterized as moving at “a solid pace”, amid “strong” job gains and “low” unemployment.

On the balance sheet, the committee said that beginning in June it will slow the pace at which it is allowing maturing bond proceeds to roll off without reinvesting them.

At the press conference, Chair Jeromy Powell reiterated that he feels monetary policy is “restrictive” and that an interest rate hike is “unlikely”, but that will be up to the data to determine and he would need “persuasive evidence” that monetary policy isn’t tight enough. “Inflation is still too high”, he said. “Further progress in bringing it down is not assured and the path forward is uncertain”.

**Chart 1: Federal Reserves Fed Fund Rates**



Source: Bloomberg, BIMB Securities

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## Rate cuts remain on the cards for 2024, but inflation progress and labor market softness is required

A combination of pent-up consumer demand, supply chain disruptions and a tight labor market sent inflation soaring to 40-year highs in 2022. The FOMC aggressively raised interest rates in 2022 and early 2023 to bring down inflation, and its efforts initially paid off in 2023. However, after trending lower throughout most of last year, inflation seems to have stiffened in 2024, leading to renewed fears the economy could slip into stagflation.

Stagflation is a phenomenon in which economic growth slows but inflation remains elevated. Given the Fed's lack of progress in bringing down inflation so far this year, many had now believed the FOMC will not pivot to rate cuts until late 2024.

Expectations around when the Federal Reserve will lower interest rates this year shifted only slightly following Chair Jerome Powell's press conference, indicating that investors' views had been in line with the bank's thinking.

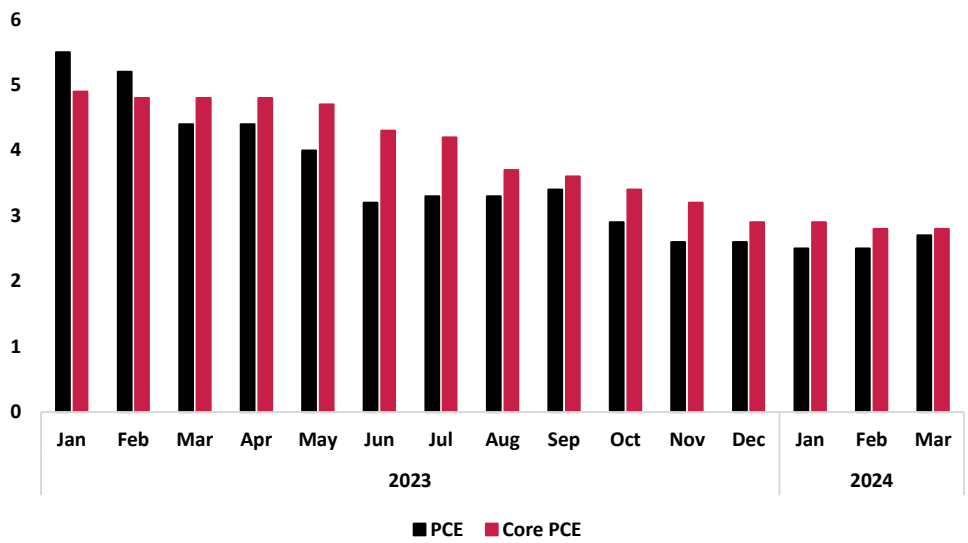
Markets are currently pricing little chance of any action at the 12 June FOMC meeting, with the odds on the CME FedWatch Tool had fallen to 9.2%. This is a remarkable swing given it was only three months ago that the market was fully expecting rate cuts this year starting at the March FOMC meeting. June cut was already off the table, July is given 25.5% chance and even September currently is no longer fully priced in. Hence, June rate cut is not happening, barring a rapid reversal of fortunes for the economy. July is also doubtful, meaning September is the more probable start point of any easing, which would limit the Fed to a maximum of just three rate cuts this year.

The CPI rose 3.5% YoY in March, up from a 3.2% annual gain in February while core CPI were up 3.8% YoY. The headline PCE accelerated from 2.5% YoY to 2.7% YoY, while core PCE price index was unchanged at 2.8% YoY. Core PCE is the Federal Reserve's preferred inflation measure, and its long-term target for core PCE inflation is just 2%. So far, the US labor market has remained resilient, giving the FOMC more leeway to keep monetary policies tight.

The odds of September and November rate cuts improved slightly following the conclusion of the Fed's policy meeting, prices of interest-rate futures indicate. There is currently a 41.2% probability of the first rate cut coming during the September meeting, according to the CME FedWatch Tool. The November meeting falls during the week of the Presidential election but Powell said there is no room for politics when "it's hard enough to get the economics right". Making decisions based on election cycles would make the Fed's already-difficult task that much harder. The CME FedWatch Tool also showed that there are now thin odds of a rate increase at some point during the year. According to CME Group, markets are currently pricing in just a 34.9% chance the Fed will issue more than one rate cut in 2024 and a 23.9% chance of no rate cut at all this year.

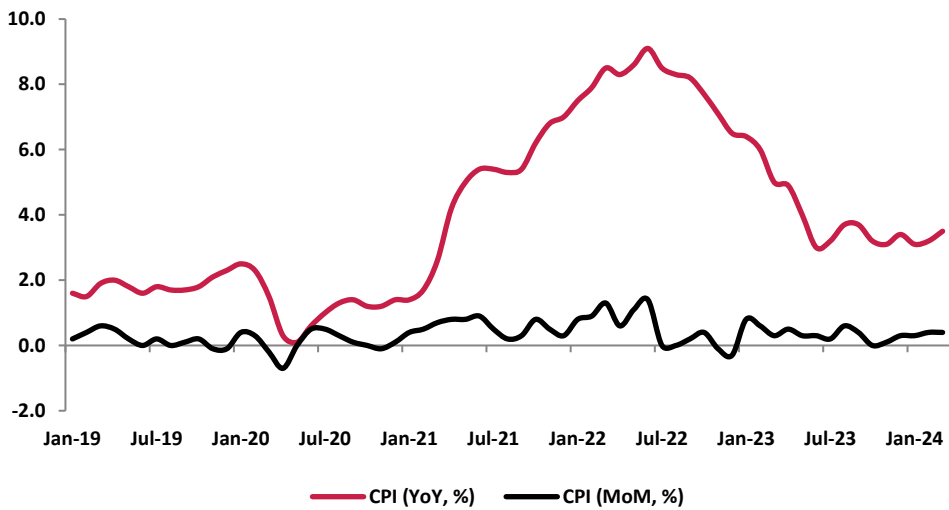
The Fed have roughly six weeks of economic data to monitor between now and the next Fed meeting in June, which could have a significant impact on monetary policy. In the near term, investors will be watching the April US jobs report on May 3 for an update on how elevated interest rates are impacting the labor market. In addition, the April CPI inflation reading on May 15 will hopefully reassure concerned investors the Fed is back on the right track and inflation is trending lower once again.

Chart 2: US PCE Inflation (%)



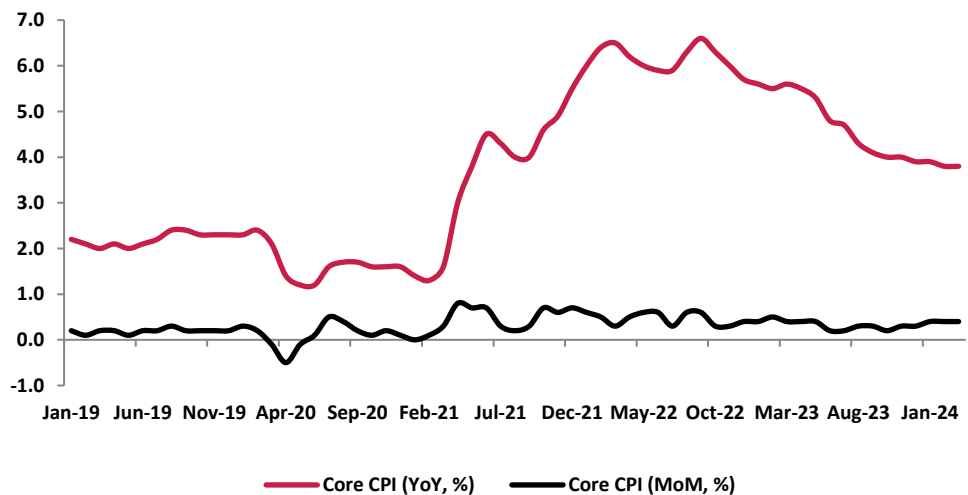
Source: Bloomberg, BIMB Securities

Chart 3: US Inflation (%)



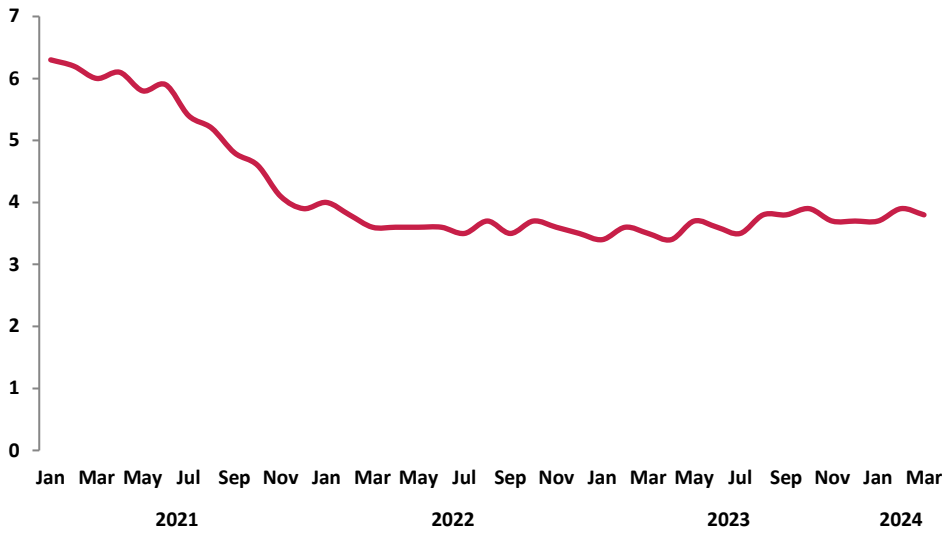
Source: Bloomberg, BIMB Securities

Chart 4: US Core Inflation (%)



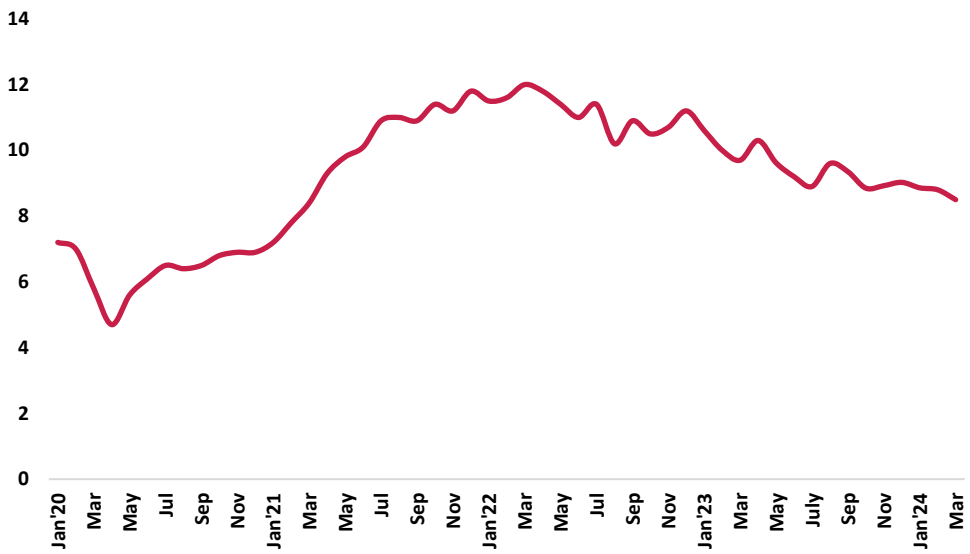
Source: Bloomberg, BIMB Securities

Chart 5: US Unemployment (%)



Source: Bloomberg, BIMB Securities

Chart 6: US JOLTS jobs opening ('million)



Source: Bloomberg, BIMB Securities

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