

# The U.S. FOMC Policy Update

Economic Update | 2nd February 2023

## Fed Slows Rate Hikes Even as Fed Says There's More Work to Do

| Event                      | Actual | Consensus | Previous |
|----------------------------|--------|-----------|----------|
| Fed Interest Rate Decision | 4.75%  | 4.75%     | 4.50%    |

### Highlights:

- The FOMC raised the benchmark rate by 25 basis points, as expected, to a target range of 4.5%-4.75%. That marks a step down from December's 50-basis-point hike and the four straight 75-basis-point moves before that.
- The committee retained its pledge to have "ongoing increases" in rates, which seems to confirm plans in the December dot plot to hike by an additional quarter point in both March and May.
- Chair Jerome Powell in his press conference all but ratified that as the current plan, saying it would take a "couple more" hikes to get to an appropriately restrictive policy.
- At their prior meeting in December, 17 of 19 policymakers forecast that they'll increase rates to 5% or above this year, with none looking for cuts. There were no fresh forecasts published on Wednesday, but Powell did reference those projections as a guide about how much higher officials expect to raise rates.
- The Fed did not issue new economic projections, but did reaffirm its commitment to its 2% average inflation target as part of its annual review of operating principles. From a peak of nearly 7% in June, the Fed's preferred measure of inflation (PCE Inflation) was 5% in December.
- Powell said for the first time the committee could conclude that the disinflationary process has started. Supply-chain improvements are helping in the goods sector and new leases point to eventual improvement in housing inflation. The big focus remains on the services sector excluding housing, where a very tight labor market may influence prices.
- Powell has drawn attention to an even narrower measure as a better guide to future price pressures — PCE core services excluding housing — which seems to be holding steady at about 4.4%.
- Powell was remarkably unconcerned about recent easing in financial conditions, pointing out he was more focused on long-term trends. He didn't take issue with market pricing of the Fed's rate path, saying it mainly reflects a market view that inflation will come down more quickly than he expects. He also sounded optimistic about the chances for a soft landing and continued good labor market.
- White House officials and the International Monetary Fund are also voicing more optimism. However, market don't think the Fed will get by without pushing the US into a downturn. Forecasters surveyed by Bloomberg in January put the probability of a contraction over the next year at 65%.

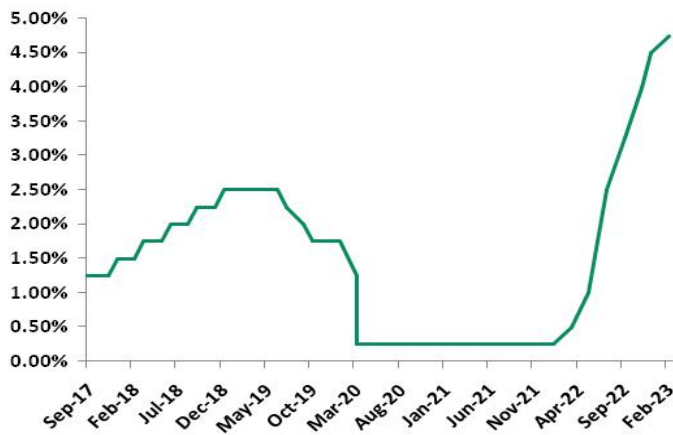
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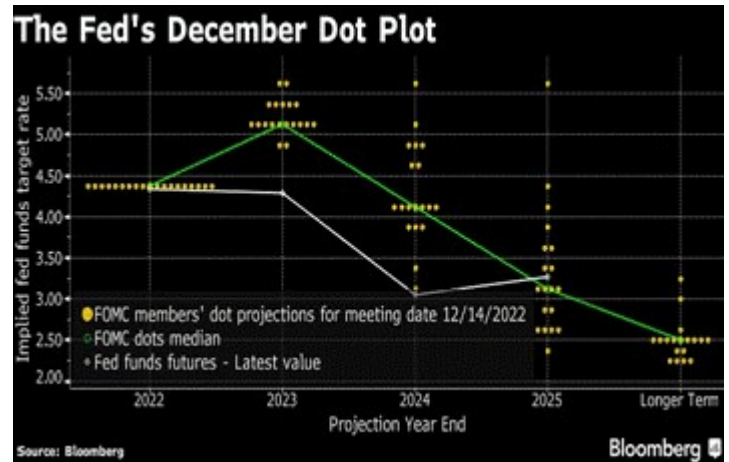
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**Fig 1: U.S. Interest Rate Trend**



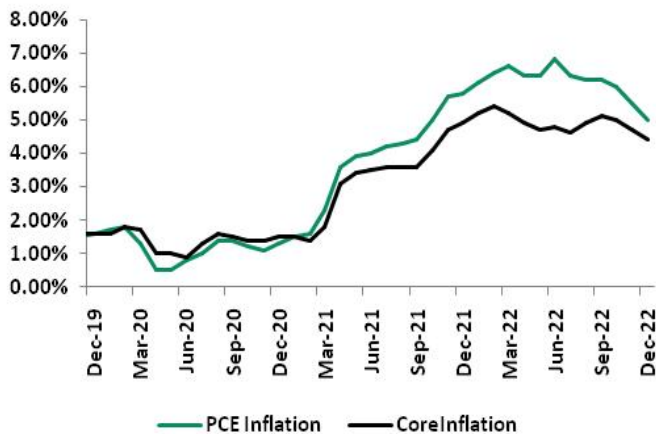
Source: FOMC, SMIFS Research

**Fig 2: FOMC December's dot plot**



Source: FOMC, SMIFS Research

**Fig 3: U.S. PCE Inflation Trend YoY**



Source: U.S. Bureau of Economic Analysis, SMIFS Research

**Fig 4: Summary of Economic Projections in December**

| Variables                              |               | Median |      |      |      |           |
|--|---------------|--------|------|------|------|-----------|
|  |               | 2022   | 2023 | 2024 | 2025 | Long Term |
| Change In Real GDP                     | Sep 22 - Proj | 02     | 12   | 17   | 18   | 18        |
|  | Dec 22 - Proj | 05     | 05   | 16   | 18   | 18        |
| Unemployment Rate                      | Sep 22 - Proj | 38     | 44   | 44   | 43   | 4         |
|  | Dec 22 - Proj | 37     | 46   | 46   | 45   | 40        |
| PCE Inflation                          | Sep 22 - Proj | 54     | 28   | 23   | 2    | 2         |
|  | Dec 22 - Proj | 56     | 31   | 25   | 2.1  | 2         |
| Core PCE Inflation                     | Sep 22 - Proj | 45     | 31   | 23   | 2.1  |           |
|  | Dec 22 - Proj | 48     | 35   | 25   | 2.1  |           |
| Projected Policy Path of Fed Fund Rate | Sep 22 - Proj | 44     | 46   | 39   | 2.9  | 25        |
|  | Dec 22 - Proj | 44     | 51   | 41   | 3.1  | 25        |

Source: U.S. Bureau of Economic Analysis, SMIFS Research

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