1 August 2024

ECONOMIC REVIEW | July 2024 US FOMC Meeting

Fed Signals Possible Rate Cut at Next Meeting as Inflation Continues to Moderate

- *Fed kept fed funds rate high as expected. After the recent meeting at end-Jul-24, the Fed's FOMC maintained the fed funds rate (FFR) at the existing range of 5.25-5.50%. The decision was widely predicted by the market consensus.*
- *More progress in inflation moving towards +2% target. In the FOMC statement, the Fed reiterated that inflation has moderated but remained "somewhat elevated". Recent data showed that there has been "further progress" in the disinflation towards the Fed's +2% target.*
- *Possible cuts as inflation eases further. The Fed Chairman signalled possibility of the Fed to begin cutting interest rates at the next meeting subject to further moderation in the US inflation.*
- *Fed to cut rates in the latter part of 2HCY24. We continue to expect the Fed to begin slashing its FFR in the latter part of 2HCY24, possibly by 1-2 rate cuts. The broad moderation in the US inflation suggests the Fed is moving closer to rate cuts.*

Fed kept fed funds rate high as expected. After the recent meeting at end-Jul-24, the Fed's FOMC maintained the fed funds rate (FFR) at the existing range of 5.25-5.50%. The decision was widely predicted by the market consensus because inflation remained above the Fed's 2% target despite renewed progress in disinflation, on the back of continued resilience in the broader US economy. The Fed also mentioned that the central bank will continue to reduce its holdings of treasury and mortgage-backed securities, where the total size of Fed's balance sheet thus far has been reduced by -USD1.76t since the recent peak in Apr-22. As of 24 July 2024, the Fed's balance sheet has decreased to nearly USD7.21t, the lowest since Nov-20.

More progress in inflation moving towards the +2% target. In the FOMC statement, the Fed reiterated that inflation has moderated but remained "somewhat elevated". Recent data showed that there has been "further progress" in the disinflation towards the Fed's +2% target. The conclusion was a change in the tone from "modest further progress" stated in the previous FOMC statement in Jun-24. Looking at the inflation data, the headline PCE inflation has eased to +2.5%yoy in Jun-24, back to the same level in Jan-Feb-24 and also the lowest since 2021. The core PCE inflation, despite remaining at +2.6%yoy in Jun-24 which was also the lowest in more than 3 years, still indicated a broad moderation in underlying inflationary pressures.

Possible cuts as inflation ease further. The Fed Chairman signalled possibility of the Fed to begin cutting interest rates at the next meeting subject to further moderation in the US inflation. While Fed has stressed the depency on incoming data to formulate its policy decision, Jerome Powell basically rejected the idea that the Fed is actively considering for a possible -50bps cut. Nevertheless, the dovish signal indicates that the Fed is approaching its first rate cut after keeping the FFR at the existing high level since the last rate hike in Jul-23.

No change to growth projection, economy still "solid"... While the Jul-24 does not come with an update to the FOMC's economic projection, the FOMC statement reiterated the solid growth in the US economy. Although the Beige Book report found more districts experienced flat or slower economic activity, the stronger-than-expected GDP growth at annualized +2.8%qoq in 2QCY24 (1QCY24: +1.4%qoq) pointed to continued resilience in the US economy backed by rebound in consumer spending on goods and more robust investment in the non-residential sector. With the US economy growing at around +3%yoy in 1HCY24, this supports the outlook that the GDP growth could expand above +2% in 2024 and could surpass the +2.1% projected by the FOMC members if job market remains robust.

The job market has returned to better balance, not a cause of inflation. The Fed Chair once again concluded that the US job market has returned to better balance, resembling the pre-pandemic conditions. With the job market rebalanced from previously tight conditions, the Fed believes the current job market situations does not pose positive pressures on the US inflation. Wage growth as measured by the average hourly earnings has eased to +3.9%yoy in Jun-24, the slowest since mid-2021. With jobless rate has risen to near 3-year high of 4.1% from the post-pandemic low of 3.4% in Apr-23, this comes with high participation rate as more people entered the job market. Job gowth remains healthy although the latest data nonfarm payrolls rose slower at +177K per month in 2QCY24 (1QCY24: +267K/month; 2023: +251K/month). The cooling labour market (and wage growth) also supports the Fed to begin easing its monetary policy as the US economy is not overheating with more balanced job market, not as tight as previously. In other words, we believe the Fed will balance its existing goal to push inflation lower and to avoid a sharp deterioration in the job market.

Americans continued to increase spending. Consumer spending remained the key component supporting the US economic growth, with retail sales growing further at +2.5% in 2QCY24 (1QCY24: +2.0%yoy). The stronger retail spending was in line with the rise in personal consumption expenditures in the 2QCY24 GDP, where Americans once again increased their spending on goods. While the still encouraging job market will continue to underpin consumption growth, consumers have expressed concerns about the short-term economic outlook amid uncertainty from high prices, upcoming election and ongoing geopolitical conflicts. Consequently, while the Conference Board consumer confidence index bounced back to 100.3 in Jul-24, the average reading in 7MCY24 at 102 was relatively weaker than average 105.4 in 2023. The University of Michigan survey also reported weaker consumer sentiment, falling to 8-month low of 66.4 in Jul-24 after trending lower in the past 4 months as consumers continued to be negatively affected by elevated inflation. In general, consumer sentiment does not show a sharp decline or a sharp increase in pessimism, therefore we foresee consumer spending will continue to grow and support the resilient economic growth this year.

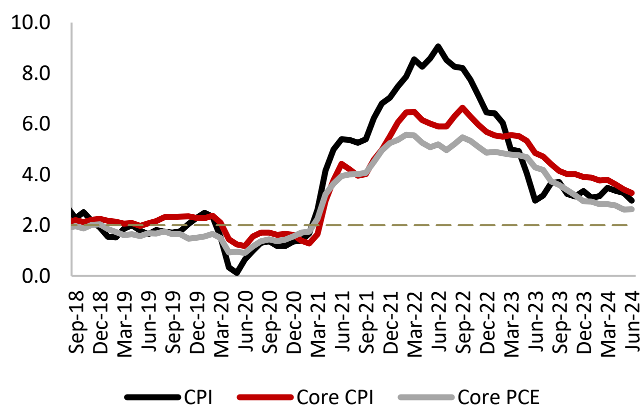
Fed to cut rates in the latter part of 2HCY24. We continue to expect the Fed to begin slashing its FFR in the latter part of 2HCY24, possibly by 1-2 rate cuts. The broad moderation in the US inflation suggests the Fed is moving closer to rate cuts. The is based on the signal from the Fed Chair that the rate cut may be done as early at the next FOMC meeting in Sep-24. However, if inflation stays stubbornly elevated, the Fed may take longer to cut its interest rate. At this juncture, we foresee a policy easing is possible this year as we see a reduced need to keep the highly restrictive policy setting for a longer period as inflation moving closer to the Fed's 2% target.

Table 1: Central Bank Policy Rate by Selected Economies (%)

	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	Apr-24	May-24	Jun-24	Jul-24
Malaysia	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00
Indonesia	6.00	6.00	6.00	6.00	6.00	6.25	6.25	6.25	6.25
Philippines	6.50	6.50	6.50	6.50	6.50	6.50	6.50	6.50	6.50
Thailand	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
Vietnam	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50
South Korea	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50
India	6.50	6.50	6.50	6.50	6.50	6.50	6.50	6.50	6.50
Japan	(0.10)	(0.10)	(0.10)	(0.10)	0.00-0.10	(0.10)	0.00-0.10	0.00-0.10	0.15-0.25
UK	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25
Euro area	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.25	4.25
US	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50

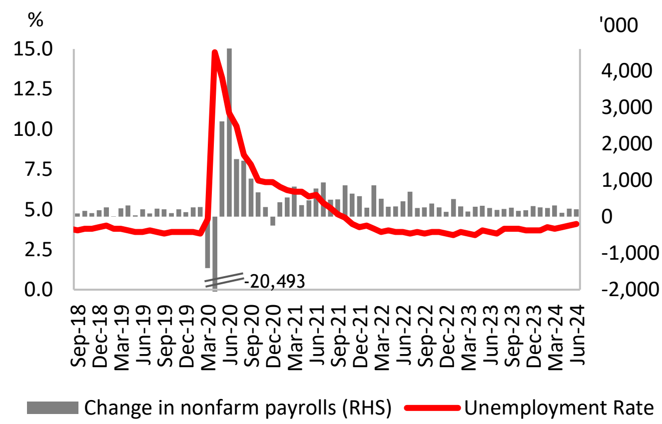
Source: Bloomberg; MIDFR

Chart 1: US CPI vs Core PCE Inflation (YoY%)



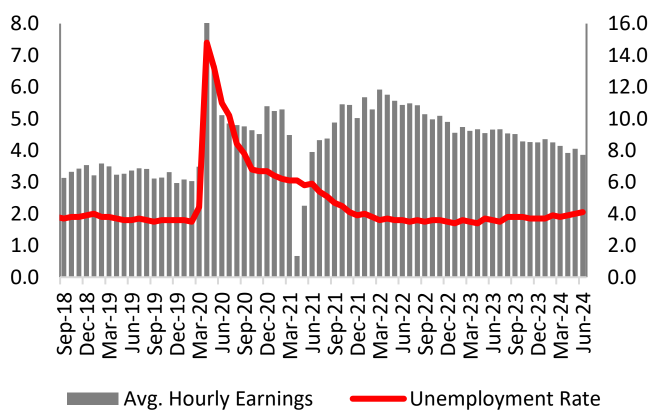
Source: Macrobond, MIDFR

Chart 2: US Unemployment Rate (%) vs Change in Non-Farm Payrolls ('000)



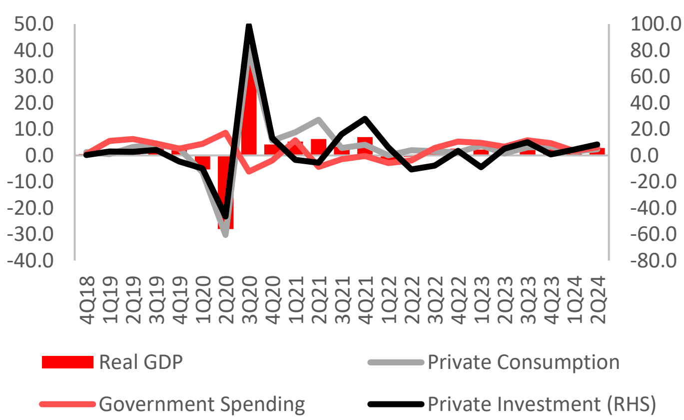
Source: Macrobond, MIDFR

Chart 3: Wage growth (YoY%) vs Unempl. Rate (%)



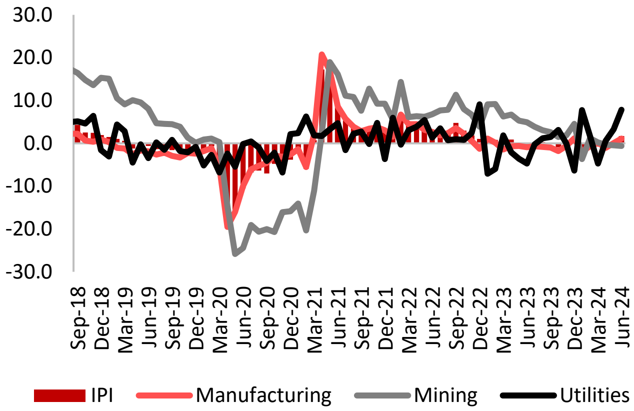
Source: Macrobond, MIDFR

Chart 4: US GDP Growth (Annualised QoQ%)



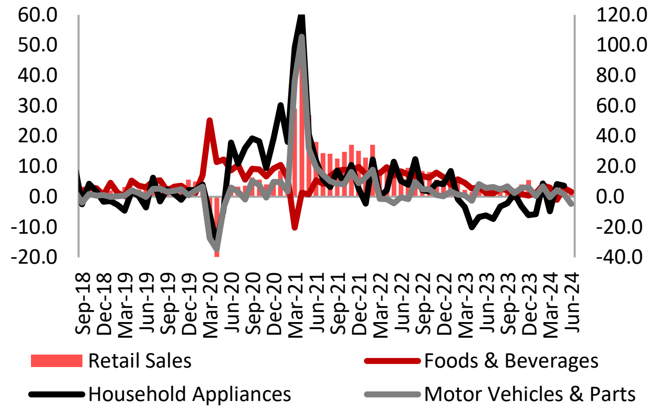
Source: Macrobond, MIDFR

Chart 5: US IPI Performances (YoY%)



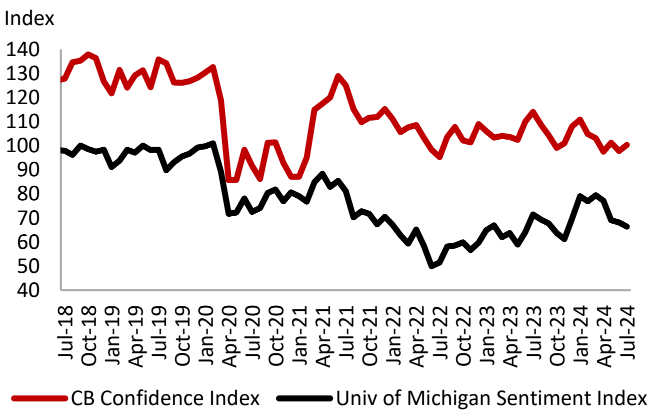
Source: Macrobond, MIDFR

Chart 6: US Retail Sales (YoY%)



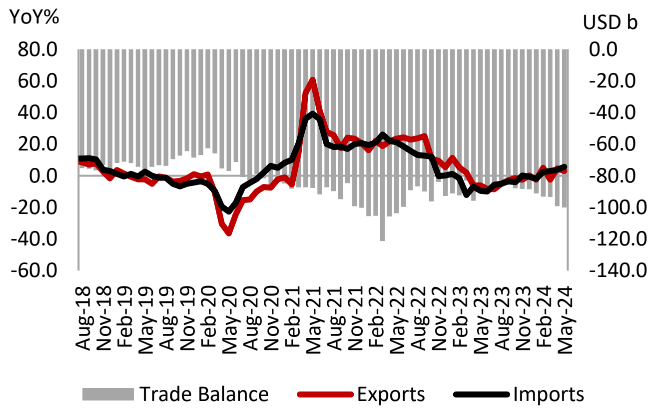
Source: Macrobond, MIDFR

Chart 7: US Consumer Sentiment & Confidence



Source: Macrobond, MIDFR

Chart 8: US Export & Import (YoY%) vs Goods Trade Balance (USD billion)



Source: Macrobond, MIDFR

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