19 December 2024

ECONOMIC REVIEW | December 2024 US FOMC Meeting

Fed Reduced Fed Funds Rate by -25bps to 4.25-4.50% and Indicated Slower Rate Cuts Next Year

- *Another -25bps cut as expected. After the Dec-24 FOMC meeting, the Fed announced additional -25bps reducing the target range for fed funds rate (FFR) to 4.25-4.50%. The decision was generally in line with the market expectations.*
- *Fed still expects inflation to ease towards its target. In the FOMC statement, the Fed reiterated the same assessment on the US inflation, which remained "somewhat elevated" despite the progress moving closer to the Fed's +2% target. Despite the recent re-acceleration in the US CPI inflation, the Fed maintained its expectation that inflation will continue to moderate.*
- *FOMC upgraded inflation projection and signaled slower rate cuts. In the updated FOMC projection, the Fed anticipated relatively higher inflation outlook. With the upgrade to inflation and growth outlook, the Fed anticipated slower rate cuts next year, with the median projection for FFR raised to 3.9% (previous: 3.4%).*
- *Fed to cut further in 2025. We maintain our expectations that the Fed will carry out 2 more rate cuts in 2025 to bring the fed funds rate closer to neutral level, in view of the broad moderation in the US inflation and further cooling in the labour market.*

Another -25bps cut as expected. After the Dec-24 FOMC meeting, the Fed announced additional -25bps reducing the target range for fed funds rate (FFR) to 4.25-4.50%. The decision was generally in line with the market expectations. The Fed Chairman indicated that the decision was a close call given the Fed's objectives to keep inflation under control (given the renewed concern of higher inflation) and support maximum employment (on the back of cooling labour market). Therefore, the Fed deemed the rate cut to be appropriate to bring interest rates closer to neutral levels. In the FOMC statement, the Fed maintained its plan to reduce holdings of treasury and mortgage-backed securities (MBS) further as part of its policy normalization. As of 11 December 2024, the size of the Fed's balance sheet shrank to USD6.90t, the lowest level last seen in early May-20. In other words, the Fed has reduced its balance sheet by -USD2.07t from the peak in Apr-22.

Fed still expects inflation to ease towards its target. In the FOMC statement, the Fed reiterated the same assessment on the US inflation, which remained "somewhat elevated" despite the progress moving closer to the Fed's +2% target. Despite the recent re-acceleration in the US CPI inflation, the Fed maintained its expectation that inflation will continue to moderate. With the core inflation remained stable, the Fed Chair also mentioned that inflation in the housing services has started to ease and this signals overall price pressures will continue to ease. Although the Fed changed its projection that the further moderation in inflation may not be as fast as previously anticipated, we expect further softening in the US inflation warrants for more policy easing by the Fed.

FOMC upgraded inflation projection and signaled slower rate cuts. In the updated FOMC projection, the Fed anticipated relatively higher inflation outlook. The FOMC upgraded its 2025 inflation projection for both the headline and core PCE inflation higher to +2.5% (previous: +2.1%) and +2.5% (previous: +2.2%), respectively, based on the median reading. This suggests the headline PCE inflation could accelerate slightly from estimated +2.4% in 2024, while core PCE inflation to moderate further but at slower rate from estimated +2.8% in 2024. In addition, the FOMC members maintained the US economic growth will remain resilient with slight upgrade to 2025 GDP growth to +2.1% (previous: +2.0%); the growth projection for 2024 was also upgraded to +2.5% from

+2.0% in the FOMC's previous projection in Sep-24. In the FOMC statement, the Fed maintained the solid expansion in the US economy. With the upgrade to inflation and growth outlook, the Fed also anticipated the pace of rate cuts will be slower, with the median projection for FFR in 2025 raised to 3.9% (previous: 3.4%). For the labour market, the FOMC anticipated little change to the jobless rate, which is projected to remain stable at 4.3% in the next 3 years albeit rising slightly from 4.2% projected for 2024.

No need for further cooling in the job market. The Fed indicated that the US job market has cooled to a loose condition, with job creation having slowed to a level the jobless rate would not remain stable (and could continue to trend higher). The previously rebalancing of the job market following the aggressive policy tightening resulted in the unemployment rate rising to 4.2% in Nov-24, gradually on the rise since from 3.4% in Jan-23. Despite the higher reading, the Fed maintained in its FOMC statement the rate still remained low. On the positive note, with no pressures from labour shortages (as labour demand has cooled), the average hourly earnings has been moderating to +3.8%yoy in 3QCY24, the slowest since mid-2021. While there is no sign of a significant deterioration in the US job market, the Fed reiterated that the job market is longer the major factor contributing to the US inflation. With no further cooling in the labour market is needed, the Fed can continue to ease its monetary policy to bring interest rates to more neutral level.

Encouraging consumer spending as confidence improved. Recent data shows consumer spending remained strong as retail sales accelerated and rose faster at +3.8%yoy in Nov-24, the fastest pace in 11 months. Apart from continued rise in job creation, consumers also indicated improved confidence on the economy despite renewed inflation expectations. This was reflected by the rise in the Conference Board Consumer Confidence Index to 16-month high of 111.7 in Nov-24. Similarly, the University of Michigan's survey reported its Consumer Sentiment Index increased further to 74.0 in Dec-24, the highest in 8 months. With improved confidence, we expect consumer spending will continue to grow and therefore sustaining growth for the US economy going forward. Nevertheless, the renewed inflation expectations support the Fed's cautious approach to future rate cuts as consumers also indicated concerns inflation could increase again.

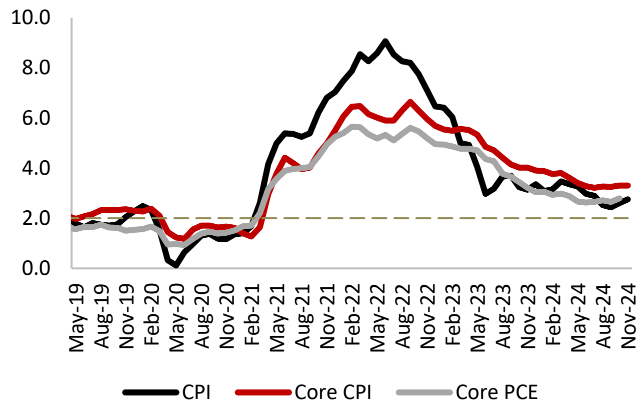
Fed to cut further in 2025. We maintain our expectations that the Fed will carry out 2 more rate cuts in 2025 to bring the fed funds rate closer to neutral level. We concur that the broad moderation in the US inflation and further cooling in the labour market provide the Fed rooms to ease further and reduce the policy restrictiveness on the economy. However, the Fed is expected to maintain a cautious stance on the pace of future rate cuts to avoid inflation from re-accelerating given the the heightened uncertainties about the inflation outlook on the back of continued strength in the US economy and renewed inflation expectations.

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

	May-24	Jun-24	Jul-24	Jul-24	Aug-24	Sep-24	Oct-24	Nov-24	Dec-24
Malaysia	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00
Indonesia	6.25	6.25	6.25	6.25	6.25	6.25	6.00	6.00	6.00
Philippines	6.50	6.50	6.50	6.50	6.25	6.25	6.00	6.00	6.00
Thailand	2.50	2.50	2.50	2.50	2.50	2.50	2.25	2.25	2.25
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	3.25	3.00	3.00
India	6.50	6.50	6.50	6.50	6.50	6.50	6.50	6.50	6.50
Japan	0.00-0.10	0.00-0.10	0.25	0.25	0.25	0.25	0.25	0.25	0.25
UK	5.25	5.25	5.25	5.00	5.00	5.00	5.00	4.75	4.75
Euro area	4.50	4.25	4.25	4.25	4.25	3.65	3.40	3.40	3.15
USA	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50	5.25-5.50	4.75-5.00	4.75-5.00	4.50-4.75	4.50-4.75

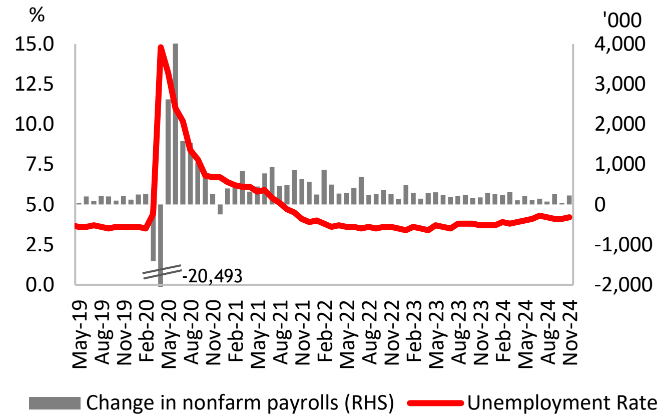
Source: Bloomberg; MIDFR

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



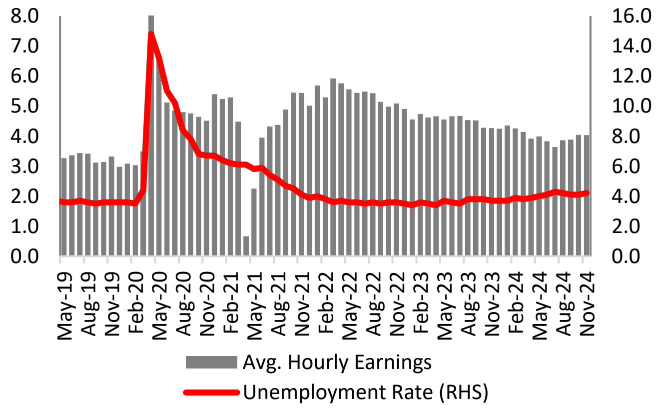
Source: Macrobond, MIDFR

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



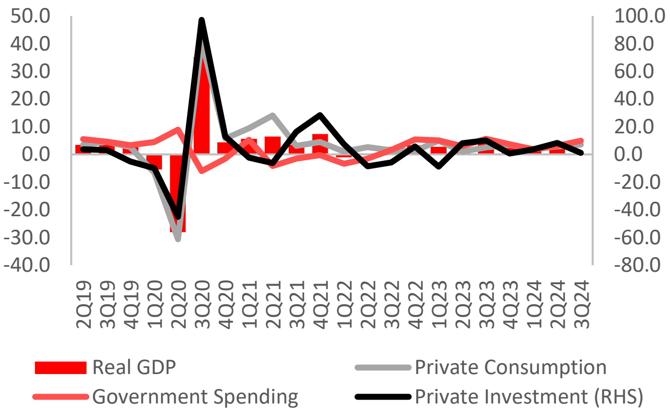
Source: Macrobond, MIDFR

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



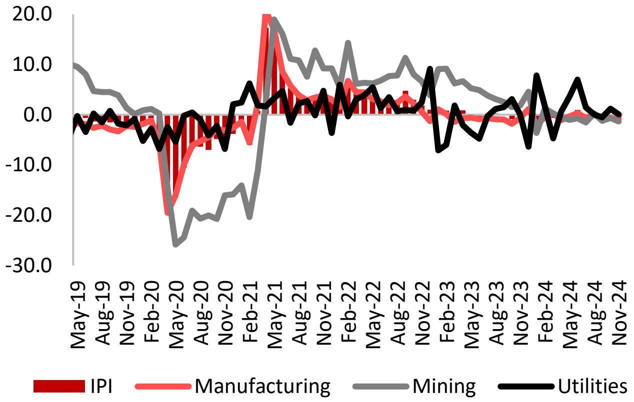
Source: Macrobond, MIDFR

Chart 4: US GDP Growth (Annualised QoQ%)



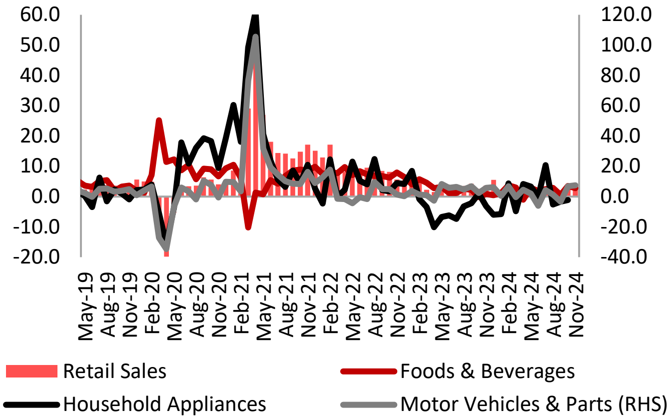
Source: Macrobond, MIDFR

Chart 5: US IPI Performances (YoY%)



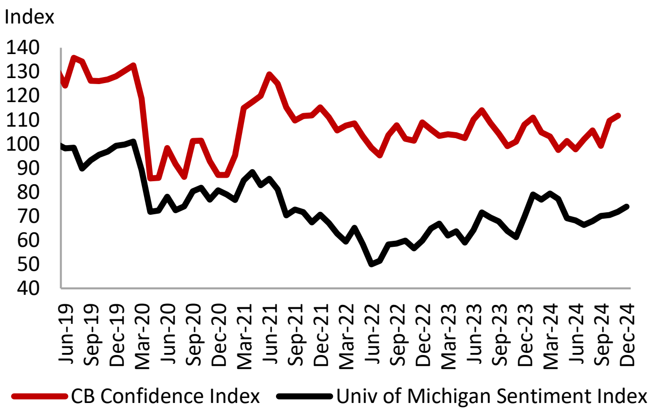
Source: Macrobond, MIDFR

Chart 6: US Retail Sales (YoY%)



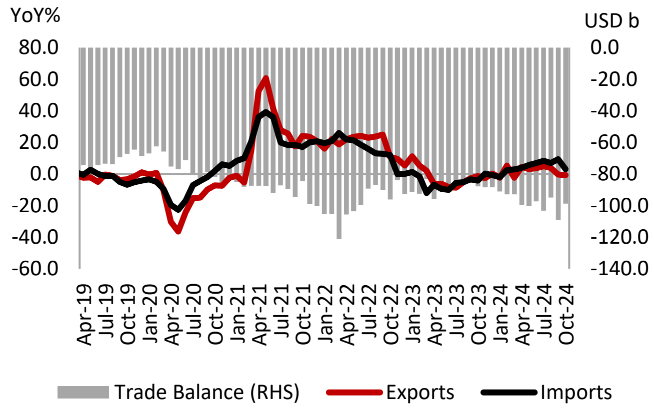
Source: Macrobond, MIDFR

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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