Daiwa Capital Markets

# U.S. FOMC Review

- FOMC: focused on inflation

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## Monetary Policy

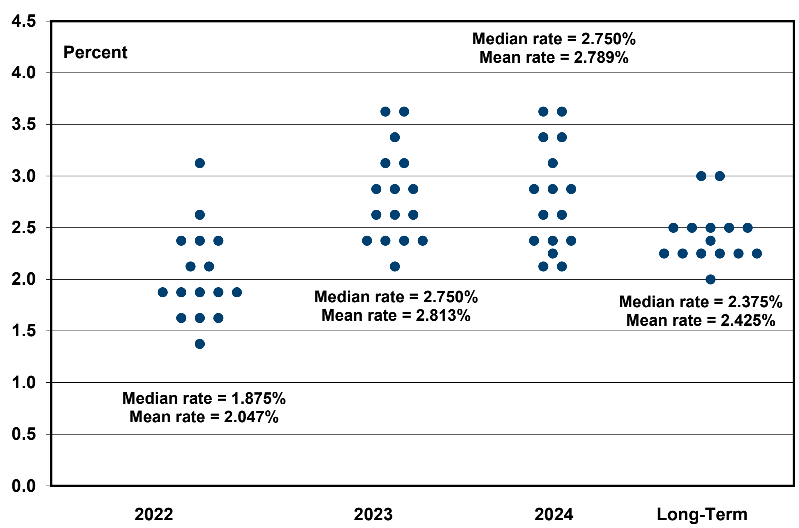
The new policy statement and the dot plot of the Federal Open Market Committee suggest that Fed officials are deeply concerned about the inflation environment. The policy statement in January attributed elevated inflation to supply and demand imbalances related to the pandemic and the reopening of the economy. The supply and demand imbalances were noted again, but so too were elevated energy prices and broader price pressures. We were especially struck by the inclusion of “broader price pressures”, as that addition could be viewed as a suggestion that policies (both fiscal and monetary) have played a role in fueling inflation.

If policy is fueling inflation, officials would need to move boldly to remove the pressure, and the dot plot indeed suggests that the Fed will be hiking aggressively. The median dot calls for a federal funds rate of 1.875 percent at the end of the year, a level that requires seven increases of 25 basis points. Going into the meeting, we were wondering if any policymaker would be looking for a federal funds rate at this level; we were shocked to see that 1.875 percent is now the central view of the FOMC. Seven officials expect the year-end federal funds rate to exceed 1.875 percent, with one official expecting a rate above three percent (chart). Such expectations will require either steps of more than 25 basis points or changes between FOMC meetings – aggressive actions. Next year, the median dot has monetary policy moving to a restrictive stance (i.e. a federal funds rate above the anticipated “long-run” reading of 2.4 percent; see the Summary of Economic Projections for the long-run view, which was revised down from 2.5 percent in December).

Chair Powell confirmed the strong hawkish tone in his press briefing. He described the economy as “very strong” and the labor market as “extremely tight”. He twice noted that officials were “acutely aware” of the importance of returning to price stability. When asked about the risk of tightening too rapidly, Mr. Powell answered that the probability of a recession was not elevated. Several times he noted that the strong economy could withstand tighter policy.

The summary of economic projections showed a noticeable slowing in GDP growth this year (a median expectation of 2.8 percent on a Q4-to-Q4 basis versus a projection of 4.0 percent in December, table). Mr. Powell described the new view as a still-

### FOMC Rate View: Year-End 2022, 2023, 2024 & Long-Term*




** Each dot represents the expected federal funds rate of a Fed official at the ends of 2022, 2023, 2024, and long-term. Normally, this graph would contain 19 projections (seven governors of the Federal Reserve Board and 12 reserve bank presidents), but three governorships wwere open at the March 2022 meeting. Moreover, only 15 Committee members provided forecasts for the long-term projection.*

*Source: Federal Open Market Committee, Summary of Economic Projections, March 2022* strong performance, one faster than the economy's potential at a time when the unemployment rate is already low – a performance that calls for the quick removal of policy accommodation.

Mr. Powell noted that the Committee made good progress in making plans for reducing the Fed's balance sheet, and that the process could begin soon, with an announcement possibly occurring after the May meeting. The Fed Chair did not provide any details on the effort, but he indicated that it would be similar to unwinding effort after the financial crisis.

## Economic Projections of the FOMC, March 2022*

| | 2022 | 2023 | 2024 | Longer Run |
|---|---|---|---|---|
| **Change in Real GDP** | 2.8 | 2.2 | 2.0 | 1.8 |
| **December projection** | 4.0 | 2.2 | 2.0 | 1.8 |
| **Unemployment Rate** | 3.5 | 3.5 | 3.6 | 4.0 |
| **December projection** | 3.5 | 3.5 | 3.5 | 4.0 |
| **PCE Inflation** | 4.3 | 2.7 | 2.3 | 2.0 |
| **December projection** | 2.6 | 2.3 | 2.1 | 2.0 |
| **Core PCE Inflation** | 4.1 | 2.6 | 2.3 | -- |
| **December projection** | 2.7 | 2.3 | 2.1 | -- |
| **Federal Funds Rate** | 1.9 | 2.8 | 2.8 | 2.4 |
| **December projection** | 0.9 | 1.6 | 2.1 | 2.5 |

** Median projections*

*Source: Federal Open Market Committee, Summary of Economic Projections, March 2022*