U.S. FOMC Review

- FOMC: pivot to lower rates initiated with a cut of 50 basis points
- The September SEP: moderate growth; expectations for inflation adjusted lower; higher near-term unemployment versus June projections
- Dot plot: 100 basis points of easing in 2024; neutral stance by 2026; median view on the long-term rate increased
- Powell press conference: "recalibration" underway; rate cuts not on predetermined course

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The September FOMC

The FOMC acted aggressively today, opting to cut the target range for the federal funds rate by 50 basis points to 4.75 to 5.00 percent. The move followed a period of heightened uncertainty among market participants about both the outcome for today's meeting and the potential path of rates that could be inferred by the Committee's action. Indeed, the Committee, too, likely debated the issue vigorously, as comments preceding the blackout period by Governor Waller and President Williams of the New York Fed appeared to lean in the direction of a more modest reduction of 25 basis points. Ultimately, those in favor of more aggressive easing carried the day, although Governor Michelle Bowman -- among the more hawkish members of the Committee -- dissented from the Committee's action in favor of a smaller cut (the first since Kansas City Fed President Esther George broke from the Committee decision at the June 2022 gathering). Moreover, uncertainty could persist for some time, as Chair Powell noted in his press conference that the first cut will not necessarily define the speed of ongoing rate reductions and that decisions will be made on a meeting-by-meeting basis.

The Committee's statement provided some insight into the policy decision. The first paragraph indicated that job gains "slowed" (versus "moderated" in the July statement) and that inflation "has made further progress" toward the 2 percent objective versus "some further progress." Additionally, the second paragraph noted that "the Committee has gained greater confidence that inflation is moving sustainably toward 2 percent," and that "risks to achieving its employment and inflation goals are roughly in balance" (versus "continue to move into better balance," previously). Thus, the third paragraph concluded "In light of the progress on inflation and the balance of risks," the Committee saw fit to lower the target range for the federal funds rate. (For a side-by side comparison of the current and previous FOMC statements, please refer to page three of this report.)

The new Summary of Economic Projections (SEP) contained several notable changes, particularly with respect to the variables that most closely inform policymakers' views on their dual mandate objectives vis-à-vis the level of the federal funds rate, as well as a new set of forecasts for 2027. With respect to the labor market, the year-end unemployment rate for 2024 (median expectation) increased to 4.4 percent from 4.0 percent in June, with expectations for the following two years also adjusted higher (table). Regarding inflation, expectations for both the headline Price Index for Personal Consumption Expenditures and the core measure were adjusted lower in both 2024 and 2025 – and a return to target was anticipated in 2026. Expectations for growth were adjusted slight lower in 2024 (median of 2.0 percent versus 2.1 percent in June) but were left unchanged in out years despite projected ongoing softening in the labor market.

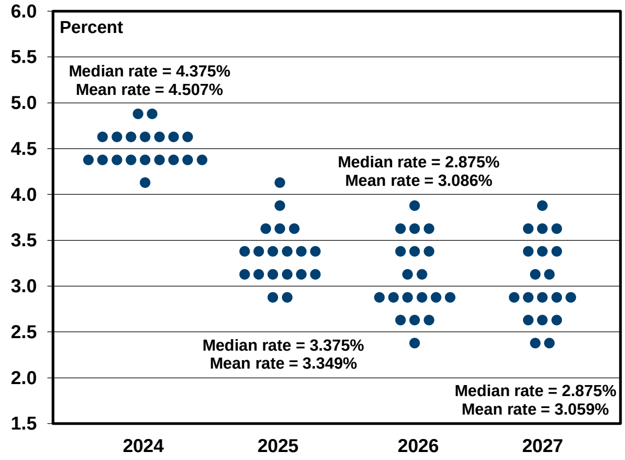
Economic Projections of the FOMC, September 2024*

	2024	2025	2026	2027	Longer Run
Change in Real GDP	2.0	2.0	2.0	2.0	1.8
June projection	2.1	2.0	2.0	--	1.8
Unemployment Rate	4.4	4.4	4.3	4.2	4.2
June projection	4.0	4.2	4.1	--	4.2
PCE Inflation	2.3	2.1	2.0	2.0	2.0
June projection	2.6	2.3	2.0	--	2.0
Core PCE Inflation	2.6	2.2	2.0	2.0	--
June projection	2.8	2.3	2.0	--	--
Federal Funds Rate	4.4	3.4	2.9	2.9	2.9
June projection	5.1	4.1	3.1	--	2.8

** Median projections*
Source: Federal Open Market Committee, Summary of Economic Projections, September 2024

In light of evolving views on the labor market and inflation, particularly with risks approximately balanced, Committee views on the trajectory of rates shifted significantly from those in the June SEP and indicated a more rapid return to a neutral stance of monetary policy (charts, below). The median projection for year-end 2024 stood at 4.375 percent, implying an additional 50 basis points in cuts by year-end (versus the previous expectation of a year-end rate of 5.125 percent). Both the latest dot plot and previous version indicated a median reduction of 100 basis points in 2025, but the year-end targets were notably different (3.375 percent in September versus 4.125 percent as of June). As of the latest SEP, the median expectation for the target range matched the longer run rate by 2026 (which was maintained in 2027).

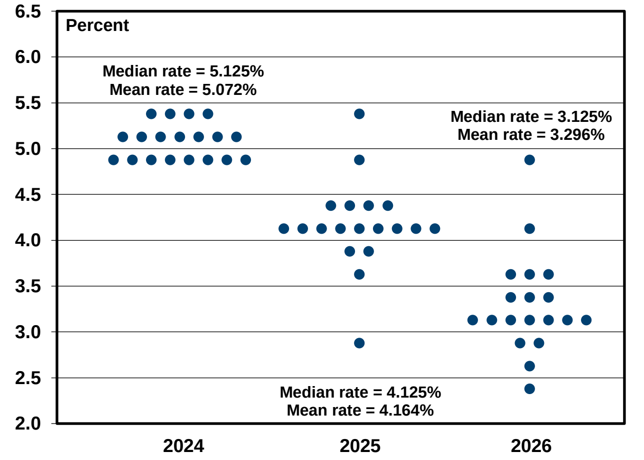
FOMC Rate View, September 2024*



** Each dot represents the expected federal funds rate of a Fed official at the end of the year.*

Source: Federal Open Market Committee, Summary of Economic Projections, September 2024

FOMC Rate View, June 2024*

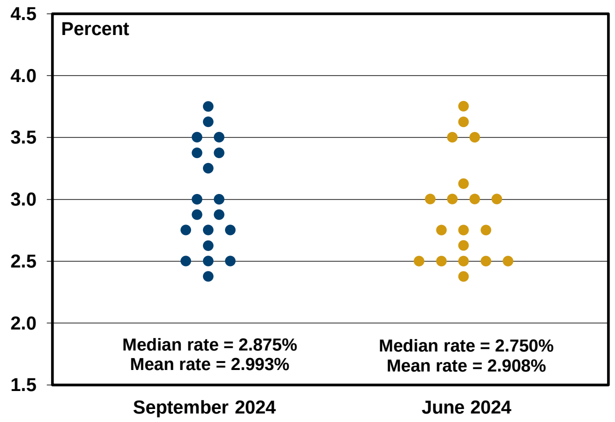


** Each dot represents the expected federal funds rate of a Fed official at the end of the year.*

Source: Federal Open Market Committee, Summary of Economic Projections, June 2024

Expectations for the longer run federal funds rate shifted higher in September (median of 2.875 percent versus 2.750 percent in June), which implies that r* (i.e. the real neutral policy rate) has continued to rise from that which prevailed earlier in the post-pandemic period (chart). However, the range of estimates remained wide at 2.375 percent to 3.750 percent, although the mean also increased somewhat versus June. Views r* ultimately have implications for where the nominal federal funds rate could settle in the next few years, but the Fed Chair's emphasis during his post-post meeting press conference on officials' ongoing reliance on the incoming data suggest that considerations regarding r* will have limited impact on near-term policy decisions.

FOMC Rate View, Longer Run*



** Each dot represents the expected longer run level of the federal funds rate of a Fed official.*

Source: Federal Open Market Committee, Summary of Economic Projections, June 2024 & September 2024

With respect to Chair Powell's press conference, discussion of a "recalibration" of monetary policy dominated. Indeed, the Fed Chair used the term several times to drive home the point that the current assessment of the balance of risks warrants a policy stance that differs from that previously required to address entrenched inflation. With that said, he stressed that the recalibration would not necessarily follow a preset course. Officials would make judgements on a meeting-by-meeting basis; another cut of 50 basis points is possible, but the first cut of that magnitude does not necessarily suggest large adjustments in the next few meetings. On the contrary, Chair Powell suggested in response to a question that the Committee "is not in a rush" to slash interest rates. That is to say, policy remains well positioned to address developments on both the inflation and employment fronts. Interestingly, though, we also would note that some concern about the labor market appeared to permeate his commentary. He noted that prior payroll growth may have been overstated (referencing the Bureau of Labor Statistics' preliminary benchmark revisions), and that future reductions in job openings could begin to translate to a pickup in layoffs; that is, future increases in the unemployment rate would be less likely to be explained away by policymakers. Even so, he emphasized reliance on the incoming data and refused to commit to another move of 50 basis points in November.

FOMC Statement Comparison*

September 18, 2024 FOMC Statement

Recent indicators suggest that economic activity has continued to expand at a solid pace. **Job gains have slowed**, and the unemployment rate has moved up but remains low. **Inflation has made further progress toward the Committee's 2 percent objective but remains somewhat elevated**.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. **The Committee has gained greater confidence that inflation is moving sustainably toward 2 percent**, and judges that the **risks to achieving its employment and inflation goals are roughly in balance**. The economic outlook is uncertain, and the Committee is attentive to the risks to both sides of its dual mandate.

In light of the progress on inflation and the balance of risks, the Committee decided to lower the target range for the federal funds rate by 1/2 percentage point to 4-3/4 to 5 percent. In considering **additional adjustments** to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. The Committee will continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities. The Committee is strongly committed to **supporting maximum employment** and returning inflation to its 2 percent objective.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

July 31, 2024 FOMC Statement

Recent indicators suggest that economic activity has continued to expand at a solid pace. **Job gains have moderated**, and the unemployment rate has moved up but remains low. **Inflation has eased over the past year but remains somewhat elevated. In recent months, there has been some further progress toward the Committee's 2 percent inflation objective**.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. **The Committee judges that the risks to achieving its employment and inflation goals continue to move into better balance.** The economic outlook is uncertain, and the Committee is attentive to the risks to both sides of its dual mandate.

In support of its goals, the Committee decided to maintain the target range for the federal funds rate at 5-1/4 to 5-1/2 percent. In considering **any adjustments** to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. **The Committee does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent**. In addition, the Committee will continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities. The Committee is strongly committed to returning inflation to its 2 percent objective.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

** Changes from statement to statement shown in bold. The vote for July 2024 was unanimous in favor of holding the federal funds rate in a range of 5.25% to 5.50%. The vote for September 2024 was 11 to 1 in favor of reducing the federal funds rate to a range of 4.75% to 5.00% (Governor Michelle Bowman dissented in favor of a smaller reduction to a range of 5.00% to 5.25%).*

Sources: Federal Open Market Committee; Daiwa Capital Markets America