3 November 2022

ECONOMIC REVIEW | November 2022 US FOMC Meeting

Fed Remains Hawkish with Another 75bps Hike, No Clear Indication on Pivot

- *Another large 75bps hike in Nov-22. After the Nov-22 FOMC Meeting, the Fed's FOMC announced another large 75bps hike, pushing the fed funds rate higher to 3.75–4.00%. This marks the fourth back-to-back 75bps increase since Jun-22, as widely anticipated by market consensus as inflation remained elevated and above the Fed's 2% longer-term target on the back of still strong labour market.*
- *Growth to be moderate in 4QCY22. According to Jerome Powell, the latest information indicates that the US economic growth would moderate in the final quarter of 2022. This is despite the rebound in US GDP growth in 3QCY22 which rose by +2.6%qoq on annualized basis (2QCY22: -0.6%), backed by increased consumer spending and amid strong job market data.*
- *Hawkish Fed to raise fed funds rate well above 4% by year-end. Given the elevated inflation and still strong labour market, the Fed is likely to push fed funds rate as high as 4.50-4.75% by end of this year. Reading from the latest Nov-22 FOMC decision and comments from the Fed Chair after the meeting, the Fed is expected to remain hawkish until there is a clear sign that inflation is trending downward.*

Another large 75bps hike in Nov-22. After the Nov-22 FOMC Meeting, the Fed's FOMC announced another large 75bps hike, pushing the fed funds rate higher to 3.75–4.00%. This marks the fourth back-to-back 75bps increase since Jun-22, as widely anticipated by market consensus as inflation remained elevated and above the Fed's 2% longer-term target on the back of still strong labour market. The FOMC also reiterated its commitment towards the balance sheet reduction plan as issued in May-22. As of last week, the Fed's balance sheet dropped to USD8.72 trillion, cumulative reduction of USD242.4b from the highest level in mid-April 2022.

No clear indication on pivot, interest rates need to be restrictive first. In response to question whether the Fed will likely pivot beyond Dec-22, the Fed Chair refused to specify any timeline whether the pace of tightening will be slowed down in the next FOMC meeting. He insists that the Fed remained focused on bringing down inflation, and the current condition requires the Fed to continue hiking rates to even higher level. In other words, the so-called terminal rate will likely be higher than what was projected in Sep-22 because inflation has yet to show any meaningful moderation, in fact inflation shows a broader price increases in the recent month. While he is satisfied with the fast pace of tightening that the Fed has carried so far, the question about which level the Fed shall stop raising rate remains uncertain. He reiterates his concern that the Fed is not doing enough in terms of tightening its policy, rather than to start withdrawing from policy tightening too soon. Chair Powell also stressed that the Fed needs to ensure the interest rates to be at 'restrictive level' to ensure inflation remains in check. At the moment, he believes there is more room for further tightening before the Fed will consider any pivot, or even pause from more hikes.

Growth to be moderate in 4QCY22… According to Jerome Powell, the latest information indicates that the US economic growth would moderate in the final quarter of 2022. This is despite the rebound in US GDP growth in 3QCY22 which rose by +2.6%qoq on annualized basis (2QCY22: -0.6%), backed by increased consumer spending

and amid strong job market data. So far, the housing market has been hit by the rise in mortgage rates, which led to the reduced private investment in the residential properties. However, Powell indicated that the adjustment in the housing market is necessary after the market had overheated following the surge in property demand previously because of the Covid-19 pandemic.

...thus narrower chance for soft landing. Nevertheless, as inflation remained high, this basically 'narrowed' the chance for the US economy to experience a soft-landing growth trajectory as the Fed is expected to continue with its policy tightening agenda. From what we understand, the Fed Chair alludes to the chance of soft-landing is still feasible if the easing of inflationary pressures can be achieved without a significant weakening of the job market (or sharp increase in unemployment) through gradual reduction in labour demand. But, this scenario becomes increasingly uncertain as the Fed will need to keep raising rates higher.

Labour market remains tight, no softening yet. One of the reasons behind the resilient and sustained growth in spending was the tight labour market, which yet to show any sign of softening. Powell mentioned that the job market has been out of balance because labour demand has been strong, exceeding than labour supply. The economy continued to add more jobs, with nonfarm payrolls increased by additional +263K in Sep-22 (Aug-22: +315K), albeit at the slowest pace since Apr-21. This kept the US unemployment rate at pandemic-low of 3.5%. Despite the aggressive tightening by the Fed this year, the US job market is expected to add another 200K jobs in Oct-22. Nevertheless, Jerome Powell did not think wage growth has been the key reason contributing to the recent uptrend in price pressures.

Rising core inflation indicates broader price pressures. The FOMC statement again indicated that there was broader price pressures as strong demand also exerting upward price pressures. The ongoing war in Ukraine remains as onf other factors that led to elevated commodity and energy prices. However, the Fed Chair mentioned that the Fed can only influence demand to limit the price pressures, which therefore require growth to be below trend and job market to soften to bring inflation towards 2% target in the longer run. Looking at the trend in both CPI and PCE prices, both core CPI and core PCE prices rose to +6.6%yoy (Aug-22: +6.3%yoy) and +5.1%yoy (Sep-22: +4.9%yoy), respectively, as inflation for items other than foods and energy rose faster in Sep-22. This again indicates the moderation in price pressures did not happen as fast as predicted.

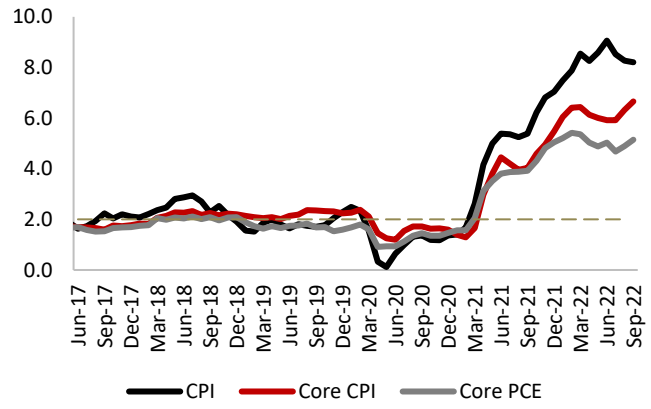
Hawkish Fed to raise fed funds rate well above 4% by year-end. Given the elevated inflation and still strong labour market, the Fed is likely to push fed funds rate as high as 4.50-4.75% by end of this year. Reading from the latest Nov-22 FOMC decision and comments from the Fed Chair after the meeting, the Fed is expected to remain hawkish until there is a clear sign that inflation is trending downward. In other words, the Fed will continue to hike fed funds rate going into next year. On the other hand, the chance for the Fed to pivot and taper down its pace of policy tightening is still possible as the US economic growth (and demand condition) are expected moderate further in 4QCY22 onwards. Nevertheless, any change in the policy direction will depend mainly on the latest trend in US inflation picture as the Fed remains focused and highly committed to bring inflation down closer to its 2% longer-term target.

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

	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22
Malaysia	1.75	1.75	2.00	2.00	2.25	2.25	2.50	2.50	2.50
Indonesia	3.50	3.50	3.50	3.50	3.50	3.75	4.25	4.75	4.75
Philippines	2.00	2.00	2.25	2.50	3.25	3.75	4.25	4.25	4.25
Thailand	0.50	0.50	0.50	0.50	0.50	0.75	1.00	1.00	1.00
Vietnam	4.00	4.00	4.00	4.00	4.00	4.00	5.00	6.00	6.00
South Korea	1.25	1.50	1.75	1.75	2.25	2.50	2.50	3.00	3.00
India	4.00	4.00	4.40	4.90	4.90	5.40	5.90	5.90	5.90
Japan	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)
UK	0.75	0.75	1.00	1.25	1.25	1.75	2.25	2.25	2.25
Euro area	0.00	0.00	0.00	0.00	0.50	0.50	1.25	1.25	2.00
US	0.25-0.50	0.25-0.50	0.75-1.00	1.50-1.75	2.25-2.50	2.25-2.50	3.00-3.25	3.00-3.25	3.75-4.00

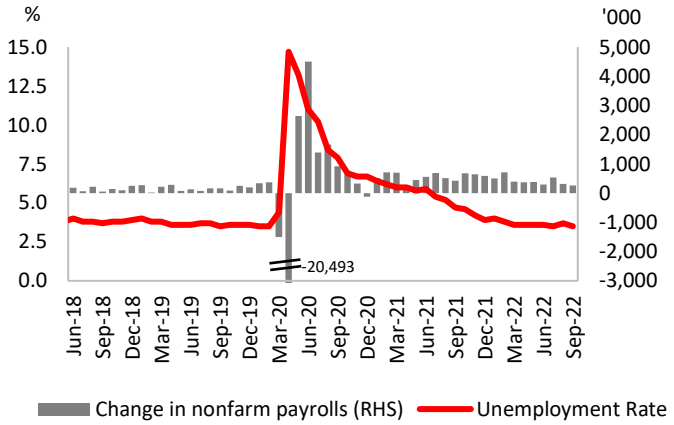
Source: Bloomberg; MIDFR

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



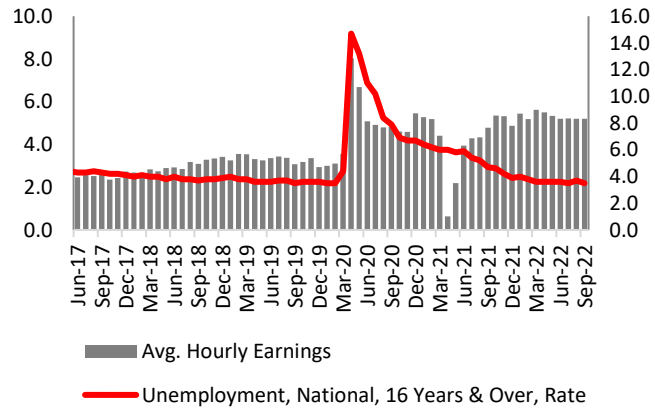
Source: Macrobond, MIDFR

Chart 2: US Unemployment Rate (%) vs Non-Farm Payroll ('000)



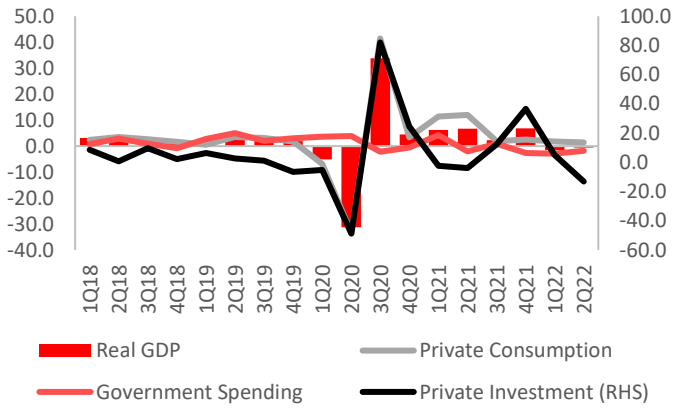
Source: Macrobond, MIDFR

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



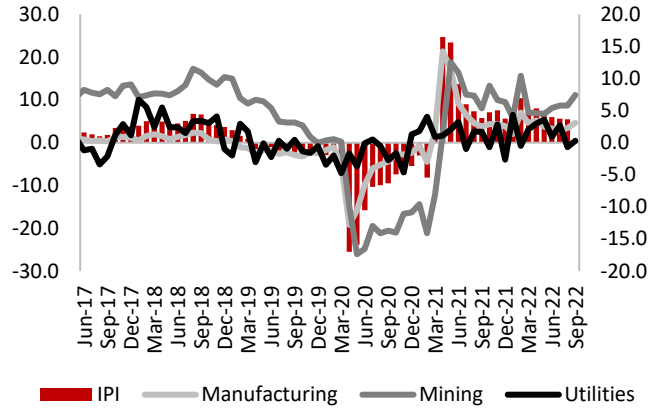
Source: Macrobond, MIDFR

Chart 4: US GDP Growth (Annualised QoQ%)



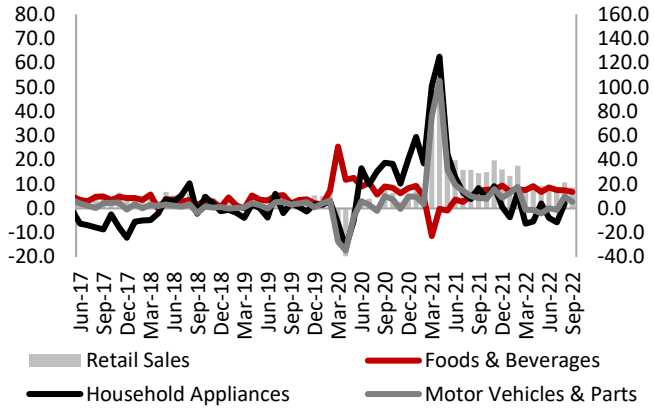
Source: Macrobond, MIDFR

Chart 5: US IPI Performances (YoY%)



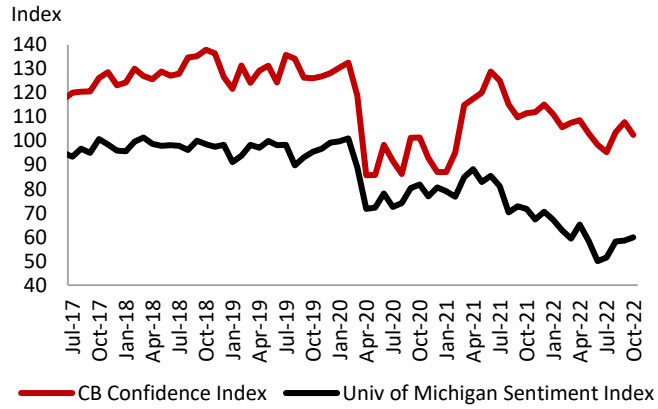
Source: Macrobond, MIDFR

Chart 6: US Retail Sales (YoY%)



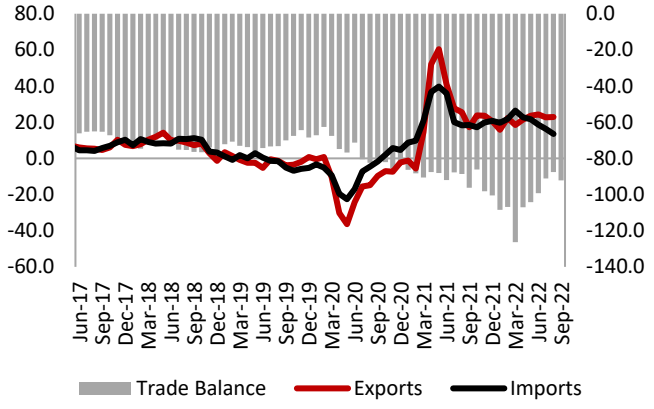
Source: Macrobond, MIDFR

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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