23 March 2023

ECONOMIC REVIEW | March 2023 US FOMC Meeting

US Fed Raised FFR by 25bps, Still Committed to Contain Inflation

- *FFR raised by 25bps as expected. In line with market forecast, the Fed's FOMC concluded its Mar-23 policy meeting by raising fed funds rate (FFR) by another 25bps to 4.75-5.00%. With inflation still exceeding its 2% longer-term target, the Fed reiterated its stance to continue policy tightening to keep inflation in check.*
- *Some tweak to the FOMC projection. There was little tweak to the Fed's forecast for US macroeconomic indicators. Based on the median forecast of the FOMC members, the latest projection predicts the US economy will grow at +0.4% this year, only a slight downward revision (Dec-22 forecast: +0.5%). The headline and core PCE inflation projected to be slightly higher at +3.3% (previous: +3.1%) and +3.6% (previous: 3.5%), respectively.*
- *Fed will continue to focus on bring down inflation. As inflation remained above the Fed's 2% target amid continued strength in the US job market, we expect the Fed will continue policy tightening to ensure inflation easing going forward. For now, we project there will be another rate hike at the May-23 FOMC meeting which could push the fed funds rate as high as 5.25%, guided by the terminal level as predicted in the FOMC projection.*

FFR raised by 25bps as expected. In line with market forecast, the Fed's FOMC concluded its Mar-23 policy meeting by raising Fed funds rate (FFR) by another 25bps to 4.75-5.00%, the highest level since 2007. With inflation still exceeding its 2% longer-term target, the Fed reiterated its stance to continue policy tightening this year and to bring rates to more restrictive levels. In fact, Chair Powell stressed about the FOMC's projection for no possible rate cuts this year, with the Fed keeping its focus to bring down inflation.

Some tweak to the FOMC projection. Although the recent economic activities were stronger than expected from Fed's perspective, there was little tweak to the Fed's forecast for US macroeconomic indicators. Based on the median forecast of the FOMC members, the latest projection predicts the US economy will grow at +0.4% this year, only a slight downward revision (Dec-22 forecast: +0.5%). The headline and core PCE inflation projected to be slightly higher at +3.3% (previous: +3.1%) and +3.6% (previous: 3.5%), respectively. The only notable difference in the latest FOMC projection is the downward revision to 2024 GDP growth, where the US economy is expected to grow below trend at +1.2% (Dec-22 forecast: +1.6%). In particular, the Fed maintained its median forecast for Fed funds rate at 5.10% this year. Even though the Fed now predicts the Fed funds rate to decline to 4.30% next year (Dec-22 forecast: 4.10%), this does not reflect a change in the Fed's thinking. In fact, the forecast is a signal that FOMC expects the policy rate will be kept at high levels before considering possible easing next year.

Banking sector still sound… While the banking sector is deemed to be "sound and resilient," the Fed highlighted that financial condition has tightened following the recent banking turmoil and this could lead to tighter credit conditions to the economy, which could affect activities the US households and businesses as well as

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job and price outlook. At this point, the Fed clearly mentioned that the extent of the impact to the economy remains unclear (i.e. too soon to be assessed), but the Fed will remain focus on managing inflation risks.

...but recent problems in the banking sector is a form of tightening. At the press conference, the Fed Chair also discussed about the initiatives taken by Fed to improve its banking supervision and regulation, in the wake of the recent bank failures affecting regional banks. He mentioned that there may be less need for further rate hikes as the stress in the banking sector also led to credit tightening. Thus, he foresees possible policy changes as a part of policy tightening without having to rely on more rate hikes. Nevertheless, more rate hikes will be considered if other policy changes do not lead to tighter financial condition.

Inflation eased but still remained high. Inflation in the US already slowed from the highs last year, with the headline CPI inflation eased to +6%yoy in Feb-23, the lowest since Sep-21. Meanwhile, core CPI inflation touched +5.5%yoy in the same month, the lowest since Dec-21. Although core PCE price inflation unexpectedly rose to +4.7%yoy in Feb-23, it is still lower than the recent peak of +5.4%yoy in Feb-22. There was no further discussion on what could keep inflation elevated in the coming months. But, the Fed looks committed in its fight to bring down inflation, still stressing on raising rates as the existing rate of inflation remained above the Fed's target.

Sign of easing wage pressures, but US labour market remained tight. Fed Chair stated that there is a sign of easing wage pressures, which had been one of the factors that pose upward pressures on general prices. Average hourly earnings rose at +4.5%yoy in the first two months of 2023 (vs. +4.9%yoy in 4QCY22). However, the job market remained strong as labour demand still high, exceeding labour supply. Unemployment rate are still at low level, despite rising to 3.6% which is still around the same level before the pandemic. The still low filings for jobless benefits indicated no sign of worsening labour market condition, although hirings decreased in the information industry. As of Feb-23, the nonfarm payrolls rose by 311K as on balance the US economy still added more jobs especially in the hospitality and retail trade sectors.

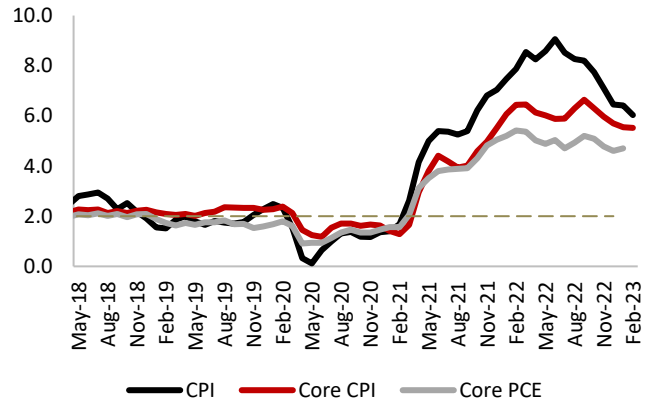
Fed will continue to focus on bring down inflation. As inflation remained above the Fed's 2% target amid continued strength in the US job market, we expect the Fed will continue policy tightening to ensure inflation easing going forward. For now, we project there will be another rate hike at the May-23 FOMC meeting which could push the Fed funds rate as high as 5.25%, guided by the terminal level as predicted in the FOMC projection. However, with the growth momentum is expected to soften in the latter part of the year, we foresee increased likelihood for policy easing towards the end of the year, which will be subject to the pace of easing in inflation and the strength of aggregate demand and overall economic growth in the latter part of the year. With the talk about tightening policy without having to resort on additional hikes, we believe the cycle of rate increases is nearing its end. On another note, as stated in our thematic report, we expect the Fed will stand ready to provide necessary supports for the US banks so that the tight liquidity condition will not become a drag to the economy.

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

	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22	Dec-22	Jan-23	Feb-23	Mar-23
Malaysia	2.25	2.25	2.50	2.50	2.75	2.75	2.75	2.75	2.75
Indonesia	3.50	3.75	4.25	4.75	5.25	5.50	5.75	5.75	5.75
Philippines	3.25	3.75	4.25	4.25	5.00	5.50	5.50	6.00	6.00
Thailand	0.50	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.50
Vietnam	4.00	4.00	5.00	6.00	6.00	6.00	6.00	6.00	6.00
South Korea	2.25	2.50	2.50	3.00	3.25	3.25	3.50	3.50	3.50
India	4.90	5.40	5.90	5.90	5.90	6.25	6.25	6.50	6.50
Japan	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)
UK	1.25	1.75	2.25	2.25	3.00	3.50	3.50	4.00	4.00
Euro area	0.50	0.50	1.25	2.00	2.00	2.50	2.50	3.00	3.50
US	2.25-2.50	2.25-2.50	3.00-3.25	3.00-3.25	3.75-4.00	4.25-4.50	4.25-4.50	4.50-4.75	4.75-5.00

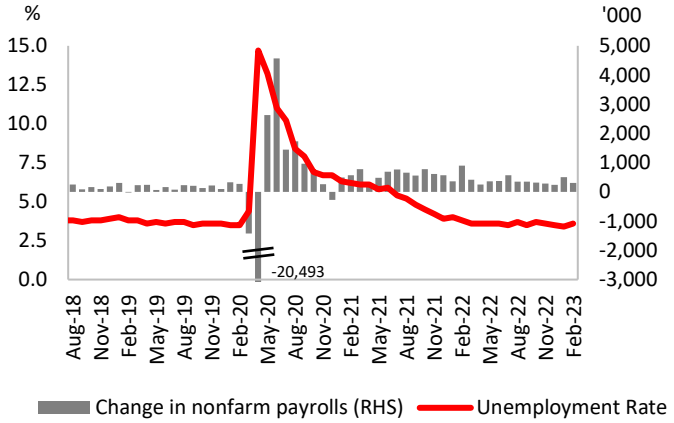
Source: Bloomberg; MIDFR

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



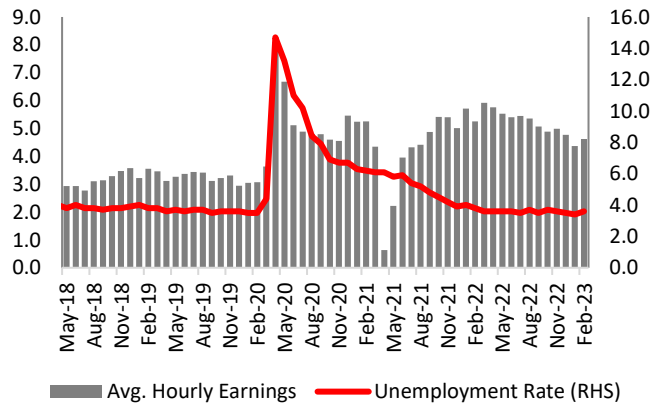
Source: Macrobond, MIDFR

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



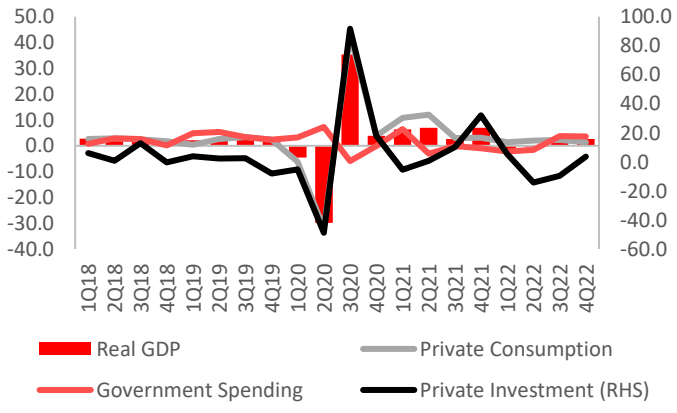
Source: Macrobond, MIDFR

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



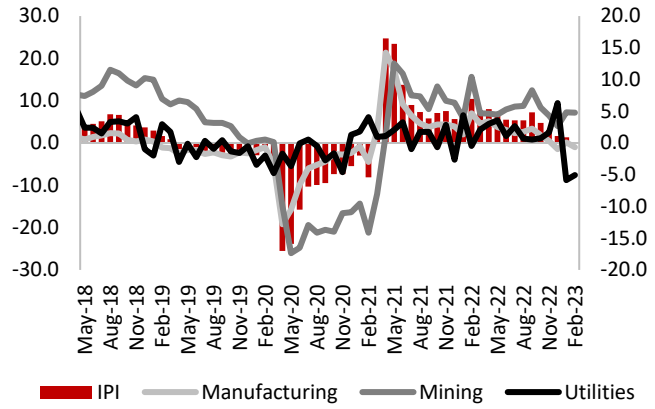
Source: Macrobond, MIDFR

Chart 4: US GDP Growth (Annualised QoQ%)



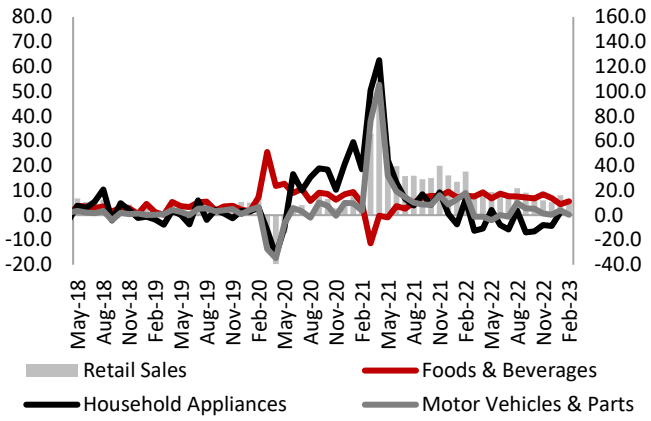
Source: Macrobond, MIDFR

Chart 5: US IPI Performances (YoY%)



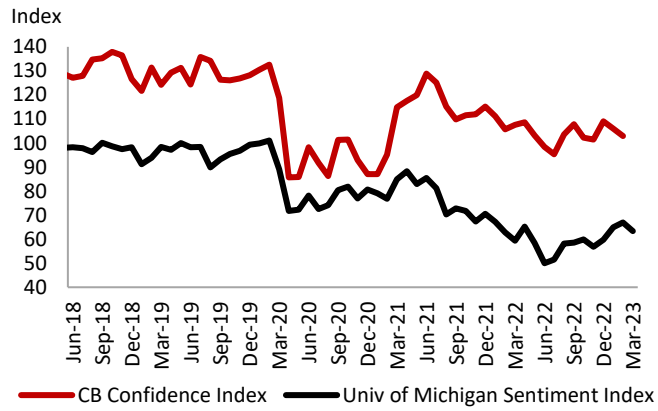
Source: Macrobond, MIDFR

Chart 6: US Retail Sales (YoY%)



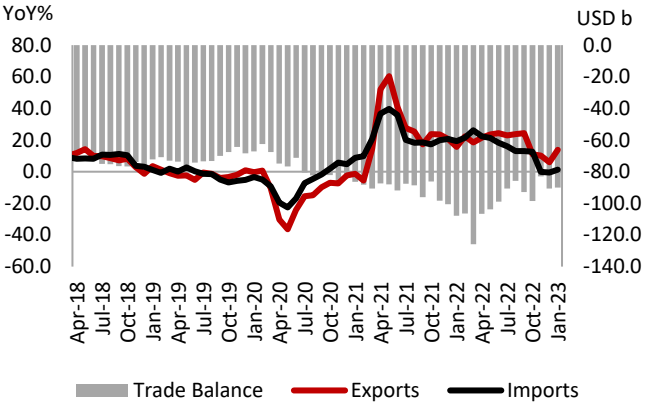
Source: Macrobond, MIDFR

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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