Fed Eases Further by -25bps, Bringing Interest Rates to Lowest Since 2022

Economic Review
Dec-25 FOMC Meeting



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- As widely anticipated, the Federal Open Market Committee (FOMC) announced the third rate cut this year, slashing the fed funds rate target by -25bps to 3.50-3.75%, the lowest level since 2022. The balancing act between supporting the job market and containing inflation supported another rate cut, moving closer to neutral level.
- The Fed also announced after the Dec-25 FOMC meeting that the Fed will initiate purchasing of short-term treasury securities as deemed necessary to ensure "ample supply of reserves". We view this as part of the decision of the Fed to end the quantitative tightening after reducing its balance sheet by more than -USD2.4t.
- The Fed Chairman reiterated concerns about the downside risks in the US job market, which affected employment and resulting in slower job growth. The heightened uncertainty about the economy and labour market is the main reason that the additional rate cuts supported by the Fed.
- We predict the Fed will deliver additional 1-2 rate cuts next year, maintaining its focus towards supporting the job market and the broader economy, with inflation is expected to ease in 2026. This, however, may be complicated by persistently elevated inflation and more resilient job market update.

Easing further to more neutral level with the Fed balancing its dual mandates

As widely anticipated, the Federal Open Market Committee (FOMC) announced the third rate cut this year, slashing the fed funds rate target by -25bps to 3.50-3.75%, the lowest level since 2022. The decision is in line with our expectations as we believe the Fed maintains its focus on supporting the economy, mainly to address concerns about greater downside risks in the job market, while nthere is nomajor spike in inflation despite higher import tariffs. According to the Fed Chairman, the division among the Fed policymakers as 3 FOMC members voted against the latest decision indicates the more balanced pressures for the Fed to keep its dual mandates to contain inflation and support full employment. In other words, the balancing act supported another rate cut, moving closer to neutral level.

Fed to short-term treasury securities to ensure ample reserves

The Fed also announced after the Dec-25 FOMC meeting that the Fed will initiate purchasing of short-term treasury securities as deemed necessary to ensure "ample supply of reserves". We view this as part of the decision of the Fed to end the quantitative tightening when the Fed decided after the Oct-25 FOMC meeting that it will end its balance sheet reduction on 1st December 2025. The size of the Fed's balance sheet shrank from USD8.97t in Apr-22 to USD6.54t as of early Dec-25, cumulative reduction of more than -USD2.4t in the Fed's holdings of treasury and agency debt securities.

Growth to strengthen next year

The FOMC concluded that the US economic activities continued to expand moderately. The updated FOMC projection, however, reflects a slight upgrade to the US GDP growth in 2025 to +1.7% (Sep-25 projection: +1.6%) with the US economy continuing to be driven by growing consumer spending. The Fed Chair indicated that the stronger GDP growth next year, upgraded to +2.3% from +1.8% previously, indicates the expected turnaround in economic growth in 1QCY26 following the reopening from the long government shutdown in 4QCY25. Apart from the reduction in borrowing costs, the US fiscal policy remains supportive of the economy.

Elevated US inflation to ease next year

The FOMC reiterated that the US Inflation remains somewhat elevated, hovering above the long-term target of +2.0%. Both the headline and core PCE prices rose at +2.8%yoy, slight re-acceleration from previous months. With no sharp spike in price pressures, the Fed anticipated that the effect from higher tariffs will be one-off and short-lived, with the FOMC projecting the headline and core PCE inflation will ease further next year towards +2.4% (2025 projection: +2.9%) and +2.5% (2025 projection: +3.0%), respectively. Apart from the fading effect of tariffs, the high base this year also supports the US inflation to moderate next year.

Cooling job market supported another rate cut

The Fed Chairman reiterated concerns about the downside risks in the US job market, which affected employment in the recent months. Although payrolls rebounded and picked up as nonfarm payrolls increased by +119K in Sep-25, the trend in recent months suggests job growth has slowed (9MCY25: +76K/month; 2024: +167.7/month). The heightened uncertainty about the economy and labour market is the main reason that supported additional rate cut by the Fed. Based on the updated projection, FOMC maintains that the US jobless rate will ease slightly to from 4.5% this year to 4.4% and 4.2% in the next 2 years.

Expect more rate cuts in 2026

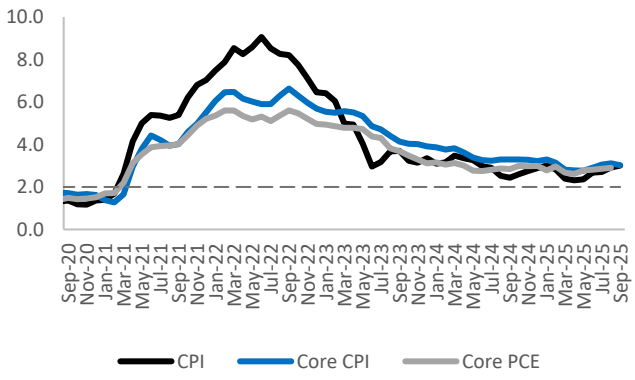
We predict the Fed will deliver additional 1-2 rate cuts next year, maintaining its focus towards supporting the job market and the broader economy, with inflation is expected to ease in 2026. Given the balanced pressures between ensuring full employment and containing inflation, the Fed has the opportunity to reduce interest rates to more neutral levels. Despite the latest projection anticipating stronger economic growth and easing inflation next year, the FOMC projection still maintains that fed funds rate will be reduced to 3.60%. Therefore, the Fed only signals 1 more rate cut next year. On another note, persistently elevated inflation and stronger job market update could delay the Fed from easing further.

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

	Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25
Malaysia	3.00	3.00	3.00	2.75	2.75	2.75	2.75	2.75	2.75
Indonesia	5.75	5.50	5.50	5.25	5.00	4.75	4.75	4.75	4.75
Philippines	5.50	5.50	5.25	5.25	5.00	5.00	4.75	4.75	4.75
Thailand	1.75	1.75	1.75	1.75	1.50	1.50	1.50	1.50	1.50
Vietnam	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50
South Korea	2.75	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
India	6.00	6.00	5.50	5.50	5.50	5.50	5.50	5.50	5.25
Japan	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
UK	4.50	4.25	4.25	4.25	4.00	4.00	4.00	4.00	4.00
Euro area	2.40	2.40	2.15	2.15	2.15	2.15	2.15	2.15	2.15
USA	4.25-4.50	4.25-4.50	4.25-4.50	4.25-4.50	4.25-4.50	4.00-4.25	3.75-4.00	3.75-4.00	3.50-3.75

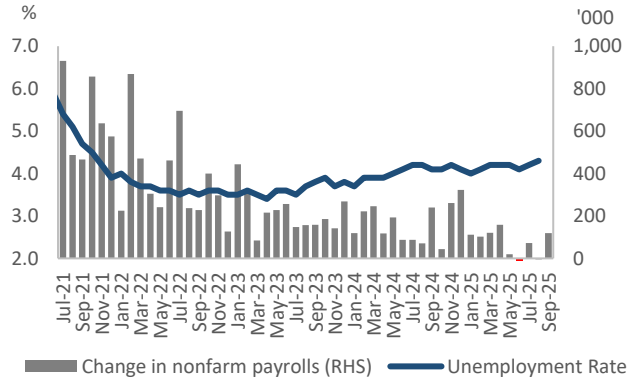
Source: Macrobond, MBSBR

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



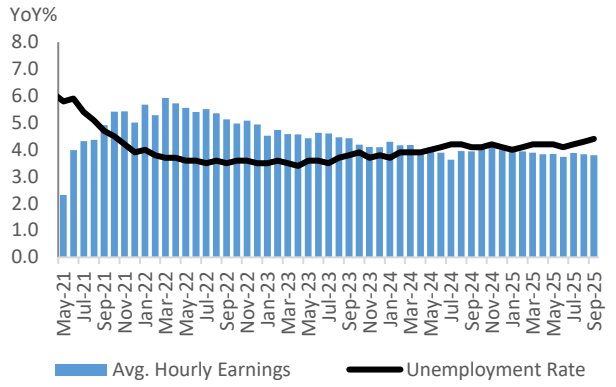
Source: Macrobond, MBSBR

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



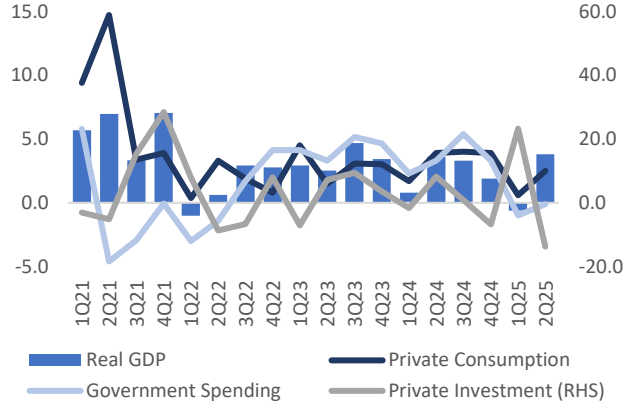
Source: Macrobond, MBSBR

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



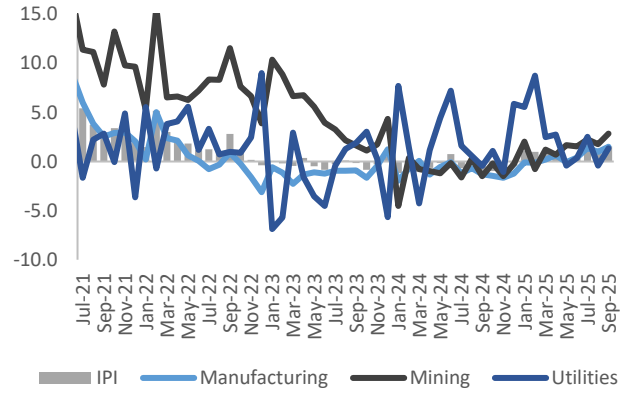
Source: Macrobond, MBSBR

Chart 4: US GDP Growth (Annualised QoQ%)



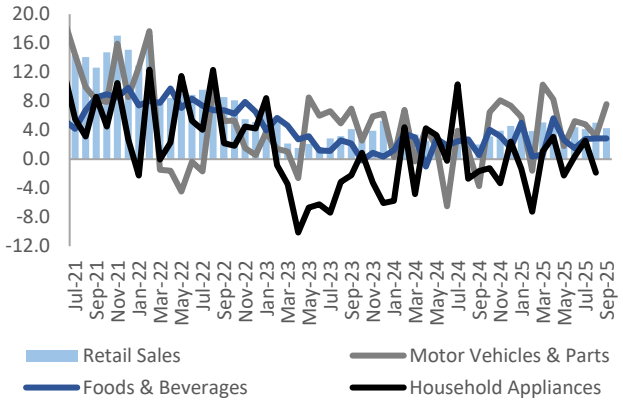
Source: Macrobond, MBSBR

Chart 5: US IPI Performances (YoY%)



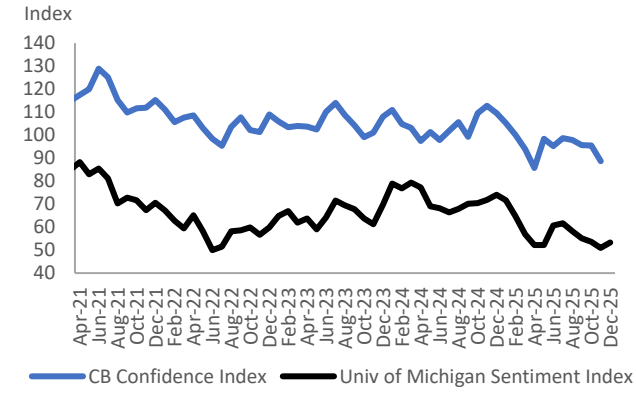
Source: DOSM, MBSBR

Chart 6: US Retail Sales (YoY%)



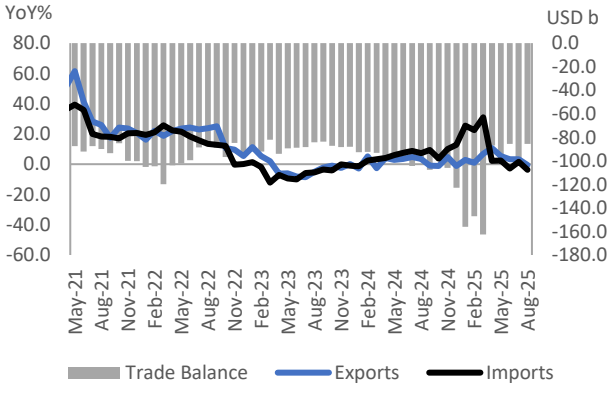
Source: DOSM, MBSBR

Chart 7: US Consumer Sentiment and Confidence (Index)



Source: Macrobond, MBSBR

Chart 8: US External Trade Performance (YoY%)



Source: Macrobond, MBSBR

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