Fed Keeps Rates Unchanged, Balancing Inflation and Job Market Concerns

Economic Review
Jan-26 FOMC Meeting



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Economic Review

- As widely anticipated, Fed maintained its policy rates. The Fed decided at the Jan-25 FOMC Meeting to keep the target range for fed funds rate (FFR) unchanged at 3.50-3.75%. The decision aligns with our expectations, as we believe the Federal Reserve remains committed to supporting economic stability.
- According to the Jan-26 FOMC implementation note, the Committee maintained the target range at 3.50% - 3.75% for the federal funds rate and the Fed will continue to engage in the purchase of shorter-term treasury securities, with up to three years of remaining maturity.
- The FOMC upgraded its economic assessment as activities in the US economy have been growing at "a solid pace." The Fed Chairman reiterated concerns about the downside risks in the US job market, highlighting that job gains have remained low, and unemployment rate showing some sign of stabilisation.
- We continue to predict as our base case that the Fed will deliver another two rate cuts for this year, focusing its policy stance towards supporting the labour market and broader economic expansion as inflationary pressures subside.

Fed balancing its dual mandates

As widely anticipated, Fed maintained its policy rates. The Fed decided at the Jan-25 FOMC Meeting to keep the target range for fed funds rate (FFR) unchanged at 3.50-3.75%. The decision aligns our expectations, as we believe the Federal Reserve remains committed to supporting economic stability; specifically by mitigating downside risks within the labour market. Crucially, this accommodative stance is bolstered by the absence of significant inflationary spikes, even in the face of elevated import tariffs. According to the Fed Chairman, the division among the Fed policymakers were lesser as 2 FOMC members voted against the unchanged decision with the preferences to lower the target by -0.25bps. In the overall basis, the Fed observe a robust expansion of economic activities but cooling labour market condition. The FOMC's emphasis on stabilisation of the unemployment rate, combined with persistent inflation, suggests a cautious approach to further rate cuts, as the economy is not yet in a recessionary state despite the slowdown in hiring.

Fed to continue purchasing short-term treasury securities to ensure ample reserves

At the January's FOMC meeting implementation note, the Committee maintained the target range at 3.50-3.75% for the federal funds rate and the Fed will continue to engage in the purchase of shorter-term treasury securities, with up to three years of remaining maturity, therefore injecting liquidity. By focusing these purchases on the short end of the curve, the Fed intends to support efficient policy implementation without signaling a return to full-scale quantitative easing.

Growth to strengthen this year

While there was no updated projection, the FOMC upgraded its economic assessment, concluding that activities in the US economy have been growing at a "solid pace." The latest view is better than the moderation expansion indicated in the previous meeting. The Dec-25 dot plot signaled the improving view to the US GDP growth for 2026. The Federal Reserve Chair noted that the upward revision of next year's GDP growth from 1.8% to 2.3% for 2026, reflects an anticipated economic rebound in 1Q26. This recovery follows the normalisation of activity after the protracted federal government shutdown in the 4Q25, which had temporarily suppressed output. Apart from the reduction in borrowing

costs, the US fiscal policy remains supportive to the economy. The latest 3Qcy25 GDP figure continue to grow at +4.4%, slightly above the initial estimate of 4.3%, marking the strongest growth since the 3QCY23.

Elevated US inflation to ease towards the end of this 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 inflation slightly accelerated to +2.8%yoy in Nov-25 (Oct-25: 2.7%yoy), while the core inflation increased to +2.8%yoy in Nov-25 (Oct-25: +2.7%yoy). 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 this year +2.4% (2025 projection: +2.9%) and +2.5% (2025 projection: +3.0%). As the impact of trade tariffs diminishes, favourable base effects from the current year are expected to facilitate a further moderation in US inflation throughout 2026. As the high price levels of 2025 drop out of the year-on-year calculations, the headline figures will likely face natural downward pressure, aiding the Fed's path toward its 2.0% objective

Cooling job market condition may support another rate cut scenario

The Fed Chairman reiterated concerns about the downside risks in the US job market, highlighting that job gains have remained low, and unemployment rate showing some sign of stabilisation. Although payrolls rebounded for the second month, as the nonfarm payrolls increased by +50k in Dec-25, however, the trend suggests job growth has slowed (12MCY25: +48K/month; 9MCY25: +76k/month; 2024: +167.7month). The heightened uncertainty about the economy and labour market is the main reason that supported for additional rate cut by the Fed. Based on the updated projection of the dot plot back in Dec-25, the FOMC's updated Summary of Economic Projections indicates that the US unemployment rate is expected to moderate slightly, moving from a projected to 4.4% in 2026 and reaching 4.2% by 2027.

Expect more rate cuts in 2026

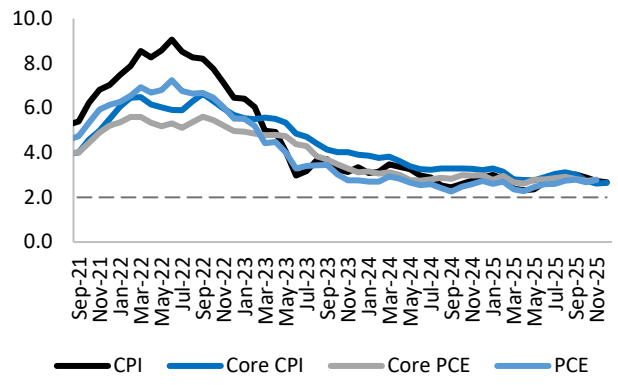
At the moment, we continue to predict as our base case that the Fed will deliver two rate cuts this year, focusing its policy stance towards supporting labour market and broader economic expansion as inflationary pressures subside. With risks to the dual mandate becoming more symmetrical, the Fed has a window to pivot toward a neutral policy rate. Based on the Dec-25 dot plot, the FOMC projection anticipating stronger economic growth and easing inflation in 2026, the FOMC projection still maintains that fed funds rate will be reduced to 3.60%, effectively signalling only one additional cut for the coming year. This outlook remains data-dependent; any resurgence in headline inflation or unexpected labour market tightening could compel the Fed to pause its easing cycle.

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

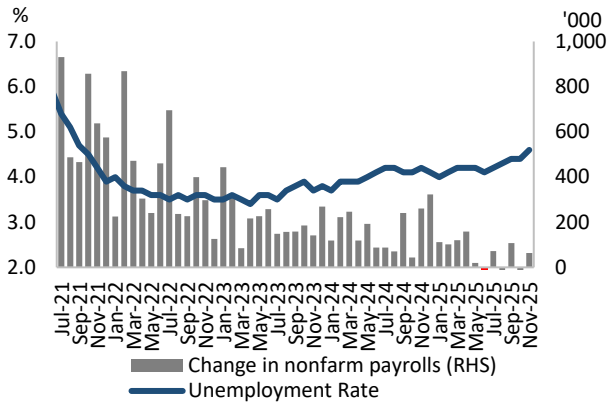
Source: Macrobond, MBSBR

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



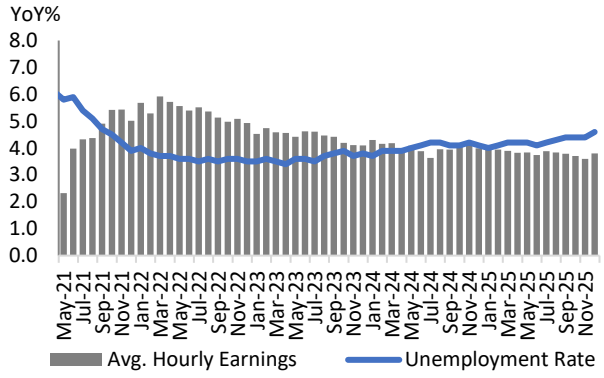
Source: Macrobond, MBSBR

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



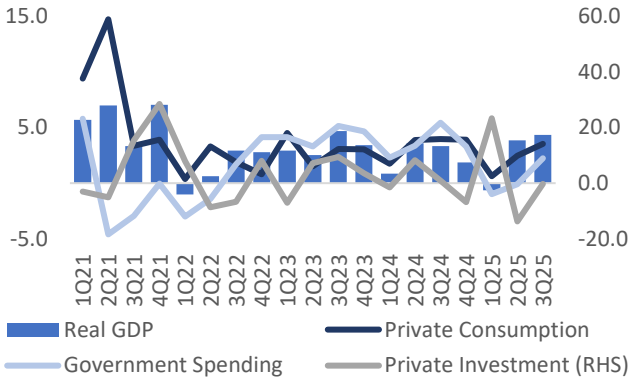
Source: Macrobond, MBSBR

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



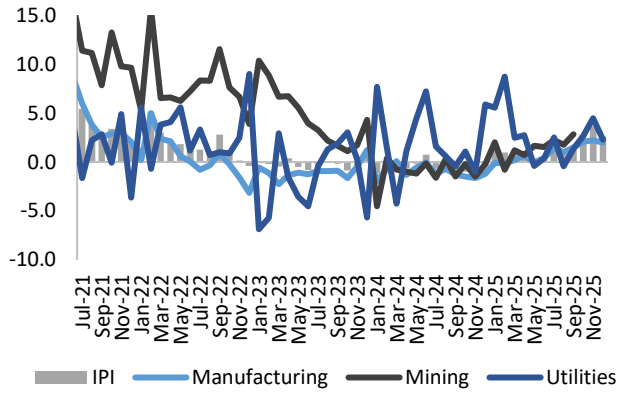
Source: Macrobond, MBSBR

Chart 4: US GDP Growth (Annualised QoQ%)



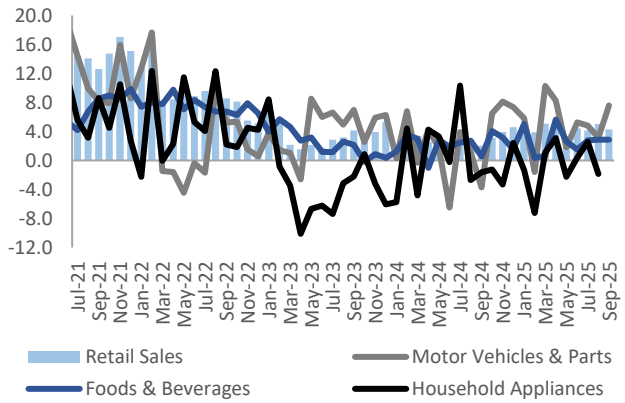
Source: Macrobond, MBSBR

Chart 5: US IPI Performances (YoY%)



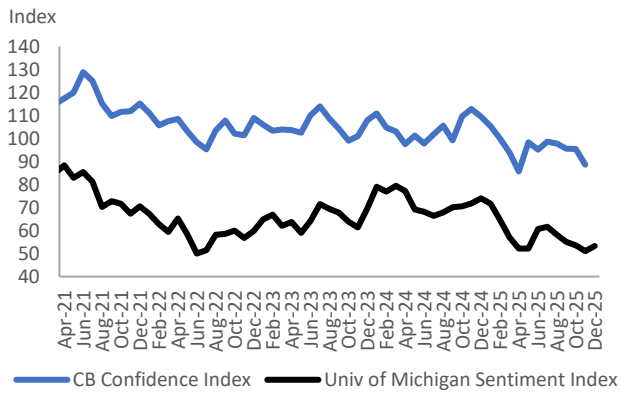
Source: DOSM, MBSBR

Chart 6: US Retail Sales (YoY%)



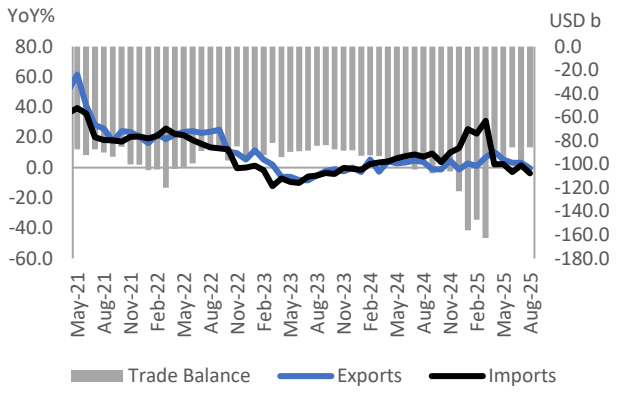
Source: DOSM, MBSBR

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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