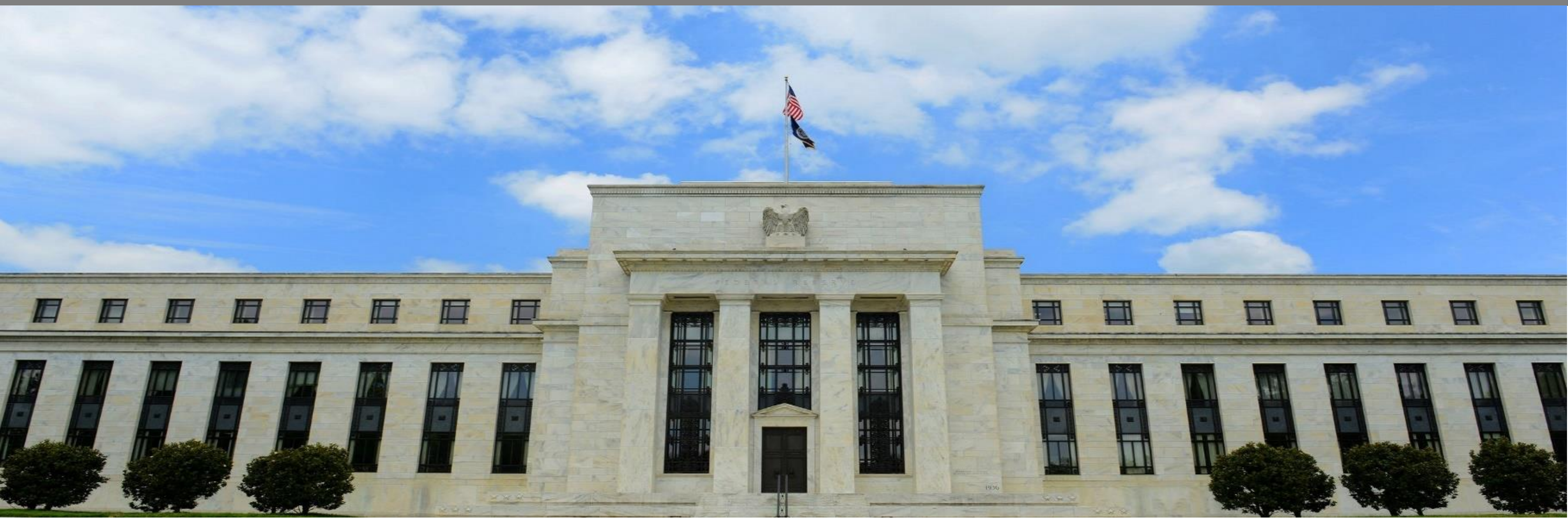
BEA 東亞銀行

Economic Research Department

19 December 2024

Economic QuickView



FOMC Meeting: The Fed adopts a hawkish stance after rate cut in December

- The FOMC voted 11-1 to reduce the Federal Funds Rate by 25 bps in December.
- The post-meeting statement and latest economic projections suggest a slower pace of rate cuts for 2025.
- The Fed's forward guidance indicates a more cautious approach due to significant uncertainties in policies, inflation, and labour market conditions.

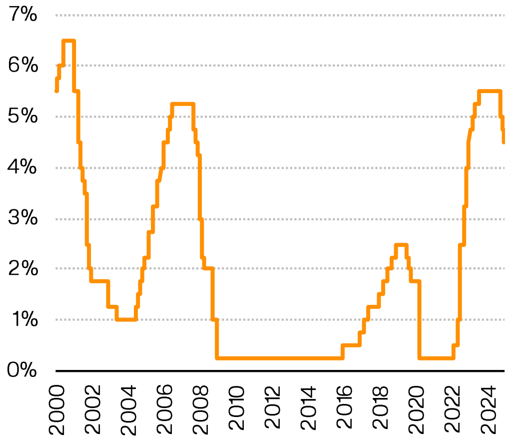
The Fed made back-to-back rate cuts in December, with one member opting for no change. At its December meeting, the Federal Open Market Committee (FOMC) voted to lower the Federal Funds Rate by 25 basis points (bps) to a target range of 4.25-4.50%. Notably, the vote was not unanimous, with one member (Beth Hammack) dissenting and preferring to maintain rates unchanged. Meanwhile, the Fed will continue to reduce its holdings of securities. The post-meeting statement added the phase "the extent and timing" when discussing future rate decisions. This hinted at a more gradual approach to rate cuts going forward, particularly following three consecutive cuts by a total of 100 bps from September to December.

December's Summary of Economic Projections (SEP) projected fewer rate cuts in 2025. In December's SEP, the median forecast for the federal funds rate at the end of 2025 was revised up to 3.875% (implying a total of 50 bps in cuts), compared to 3.375% (a total of 100 bps in cuts) in September's SEP. December's Dot Plot for 2025 also showed a marked upward shift, with 14 out of 19 FOMC members projecting rates at 3.875% or above, compared to just 2 members in September. In addition, the longer-run neutral rate was revised up to 3.0% in December, from 2.875% in September. While the projections for GDP growth and the unemployment rate were little changed, the median forecasts for core PCE inflation were revised up to 2.8% in 2024, 2.5% in 2025, and 2.2% in 2026, from September's projections of 2.6% for 2024, 2.2% for 2025, and 2.0% in 2026. These revisions suggest that inflation risks probably led the FOMC to project a slower rate cut path in 2025.

FOMC Projections (December 2024)	2024	2025	2026	2027	Longer run
Real GDP growth (%) [September 2024]	**2.5** [2.0]	**2.1** [2.0]	**2.0** [2.0]	**1.9** [2.0]	**1.8** [1.8]
Unemployment rate (%) [September 2024]	**4.2** [4.4]	**4.3** [4.4]	**4.3** [4.3]	**4.3** [4.2]	**4.2** [4.2]
Core PCE inflation (%) [September 2024]	**2.8** [2.6]	**2.5** [2.2]	**2.2** [2.0]	**2.0** [2.0]	-
Fed Funds rate (%) [September 2024]	**4.4** [4.4]	**3.9** [3.4]	**3.4** [2.9]	**3.1** [2.9]	**3.0** [2.9]

Source: The Fed

US Fed Funds Rate (Upper)



Source: Bloomberg

Fed Chairman Jerome Powell signalled a more intensive focus on inflation and a more cautious approach to rate cuts going forward. During the post-meeting news conference, Fed Chairman Jerome Powell described that the Fed is in a new phase in its monetary policy adjustments. While rates remain restrictive, the rate level is now closer to neutral following cuts totalling 100 bps. Additionally, inflation has been moving sideways in recent months. These developments call for the Fed to move forward cautiously and look for further progress on inflation. Moreover, he confirmed that some of the FOMC members took a preliminary step to incorporate the potential economic effects of future policies into their forecasts. This was in line with the consensus view that certain policies advocated by President-Elect Donald Trump could add inflationary pressure to the US economy, such as higher tariffs, tax cuts, and mass deportations of illegal immigrants.

Markets rapidly priced in a narrative of a higher-for-longer rate outlook amid the Fed's hawkish pivot. After the FOMC decision, the S&P 500, Dow Jones, and Nasdaq all fell by 2.95%, 2.58%, and 3.56% on 18 December, while Treasury yields and the US dollar surged. This reflected reduced rate cut expectations with a heightened risk-off mood. In our view, the shift in the Fed's forward guidance reflects a more cautious approach amid significant uncertainties in policies, inflation, and labour market conditions. We expect that the Fed is likely to slow its pace of rate cuts in 2025, depending on economic data and Trump's policy implementation. Meanwhile, banks in Hong Kong reduced their prime rates by 12.5 bps. For 2025, prime rates are likely to follow the path of US interest rates, albeit at smaller reductions.

BEA 東亞銀行

Economic Research Department **19 December 2024**

Disclaimer

For more information, please visit our webpage at https://www.hkbea.com/html/en/bea-about-bea-economic-research.html. For any enquiries, please contact the Economic Research Department of BEA (email: lerd@hkbea.com/telephone number: (852) 3609-1504/postal address: GPO Box 31, Hong Kong).