Metrobank

Research and Market Strategy Department

POLICY RATE VIEWS

FED SIGNALS ONE CUT IN 2024, KEEPS DOOR OPEN FOR TWO

Fed Action

The US Federal Reserve (Fed) maintained the Federal Funds Target Rate (FFR) at 5.25% - 5.50% for the seventh consecutive time during its Federal Open Market Committee (FOMC) meeting yesterday, June 12, 2024. This comes after a string of 11 prior rate hikes, including four hikes in 2023.

Fed Signals

The FOMC noted there has been a "modest further progress towards the committee's 2% inflation objective" in recent months, an adjustment to their previous statement that pointed to a "lack" of further progress on inflation.

Although the Fed's latest dot plot indicated a single 25-basis point (bp) cut this year, Fed Chair Jerome Powell maintained his dovish tone and mentioned one to two cuts are plausible this year.

Fed officials continued to state that interest rates are likely to stay elevated for longer after price pressures picked up in the first quarter, but they acknowledged the softer inflation trends since then. In particular, Powell cited the May print as "progress in building confidence" on US inflation's downward trajectory.

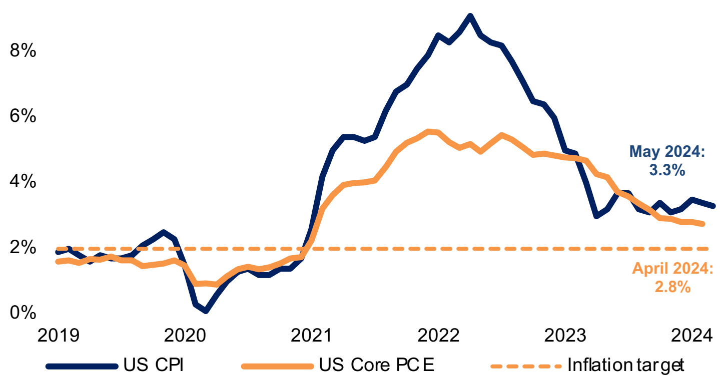
Chair Powell also described the overall labor market as strong but gradually cooling, comparing it to the state of the jobs market at the cusp of the pandemic. However, an unexpected weakening could warrant a response by the Fed.

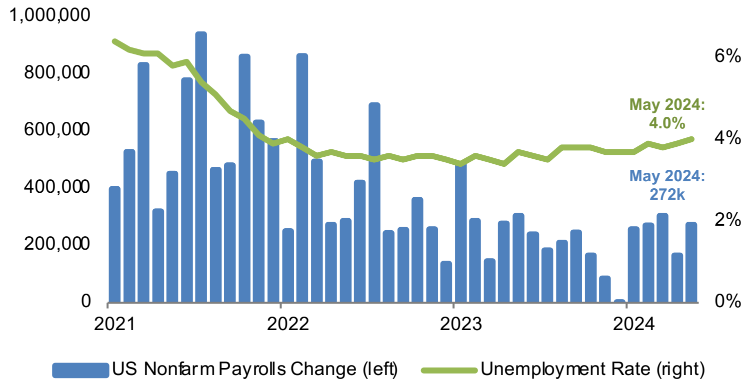
While officials have lightly raised their forecast for long-run interest rates, officials are still waiting to see sufficient progress prior to easing. Powell also believes that the evidence is "pretty clear" that the effects of the restrictive monetary policy is currently being felt in terms of reining in demand and bringing the economy, including inflation, back into better balance.

Fed Funds Target Rate as of June 13, 2024

5.25% to 5.50%

US Economic Data





US headline inflation fell flat on a month-on-month (MoM) basis in May, slower than the 0.1% consensus estimate and the 0.3% print recorded in the previous month. Year-on-year (YoY), it accelerated at 3.3%, slower than the 3.4% consensus estimate for the month and actual print recorded in April. While overall food prices were up 0.1% MoM, the slower-than-expected acceleration in US inflation was mainly attributed to the 3.6% MoM drop in gasoline prices for the month.

Notably, US core services inflation rose only 0.2% MoM in May, the slowest since September 2021, cementing the Fed's footing in its fight for disinflation. This was mainly due to a 0.5% price deceleration in transportation services as airline prices dropped by 3.6% and motor vehicle insurance similarly declined by 0.1%, all relative to the previous month.

Moreover, the Fed's preferred inflation gauge, the core Personal Consumption Expenditures (PCE) index, came in at 0.25% MoM in April from the previous month's 0.33%. On a year-on-year basis, it was recorded at 2.75%, slightly slower than the 2.81% recorded in March.

On the US labor market, the recent nonfarm payrolls report in May reported a surprise increase of 272,000 new jobs, which was substantially higher than the 180,000 consensus estimate. A large volume of these jobs came from the Education and Health Services Sector. Meanwhile, the unemployment rate increased to 4.0% versus a consensus estimate of 3.9%.

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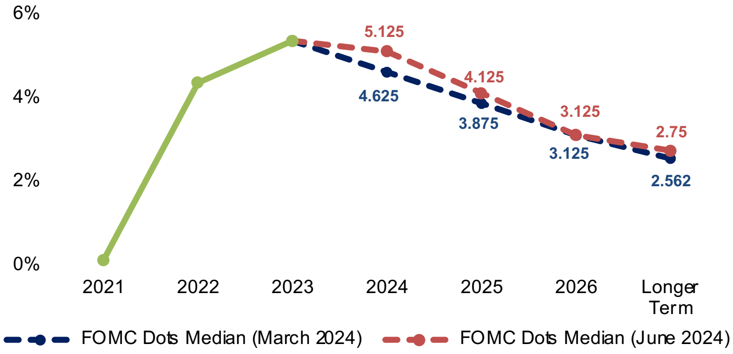
POLICY RATE VIEWS

FED'S ECONOMIC PROJECTIONS

US Federal Reserve's Economic Projections (in %)	as of March 2024				as of June 2024			
	2024	2025	2026	Longer run	2024	2025	2026	Longer run
Real GDP	2.1	2.0	2.0	1.8	2.1	2.0	2.0	1.8
Unemployment Rate	4.0	4.1	4.0	4.1	4.0	4.2	4.1	4.2
PCE Inflation	2.4	2.2	2.0	2.0	2.6	2.3	2.0	2.0
Core PCE Inflation	2.6	2.2	2.0		2.8	2.3	2.0	



The accompanying Summary of Economic Projections (SEP) of the Fed pointed to a median projection of only one 25-bp cut in 2024, down from three cuts in the last SEP in March. Of the 19 voting FOMC members, 7 voted in favor of one cut this year, 4 voted for no cuts, while 8 favored two cuts or a total of 50-bps. The June SEP also revealed that the FOMC is projecting a higher terminal Fed Funds rate at 2.75% in the longer term, compared to the previous projection of 2.562% last March.

FORECAST & OUTLOOK

Although the Fed dot plot currently indicates only a 25-bp cut in 2024, the additional 25-basis point (bp) cut which is now projected to be rolled over to 2025 has reassured the markets of a 125-bp cut within the 2-year horizon. With this, US Treasury Yields ended 6-10 bps lower across all tenors after the FOMC meeting, with the 2-year yield 8 bps lower at 4.7518%.

Metrobank Research maintains its view that the Fed may begin cutting rates as early as its September 18 FOMC meeting and by a total of 50 bps for the full-year to 4.75% - 5.00% as inflation is expected to have peaked by June and July, observable by August.

Albeit there were upward adjustments in the Fed's inflation projections, we still see no signs of inflation re-accelerating in the US, unlike in the Eurozone, as both the Consumer Price Index (CPI) and the Core Personal Consumption Expenditures (PCE) have moderately eased in the past two months and is projected to continue easing gradually in the coming months.

Metrobank Research reaffirms its view that the Bangko Sentral ng Pilipinas (BSP) may begin its own easing cycle in the fourth quarter, lagging the Fed's first policy rate cut to support the peso. Given the new projections on US policy rate, we now forecast a total of 50 bps in cuts for the year to 6.0%, down from our previous projection of 75 bps.