Metrobank

Research and Market Strategy Department

POLICY RATE VIEWS

GO BIG OR GO HOME: FED CUTS BY 50 BPS

Fed Action: "Dovish" upsized 50bp cut

The US Federal Reserve (Fed) reduced the Federal Funds Target Rate (FFR) by 50 basis points (bps) to 4.75% - 5.00% during the Federal Open Market Committee (FOMC) meeting on September 17-18. Prior to this, markets were pricing in a median of a 40-bp cut, implying more players expected a 50-bp cut for the September meeting. Powell emphasized this may not be the "normal" with regard to easing. This was the first adjustment for the FOMC after holding policy rates steady for eight consecutive meetings.

Fed Focus: Jobs

In the September FOMC statement, the committee recognized that job gains have slowed and that inflation, which remains somewhat elevated, has made further progress toward the 2% target.

FOMC Chair Jerome Powell recognized this in his opening speech, where he highlighted a strong overall US economy that has made significant progress towards the FOMC's goals over the past two years. In particular, the FOMC chair pointed to the "cooling" labor market which has gained an average of 116 thousand payroll jobs over the past three months, notably lower than in the earlier months this year, as well as inflation, which has "eased substantially" to 2.2% in August from the peak of 7%.

The FOMC chair also emphasized that the committee would continue to assess incoming data and the evolving outlook, recognizing that a hastened monetary easing could hinder progress on inflation, while a slow reduction in policy rates could weaken growth and employment.

Fed Funds Target Rate as of September 19, 2024

4.75% to 5.00%

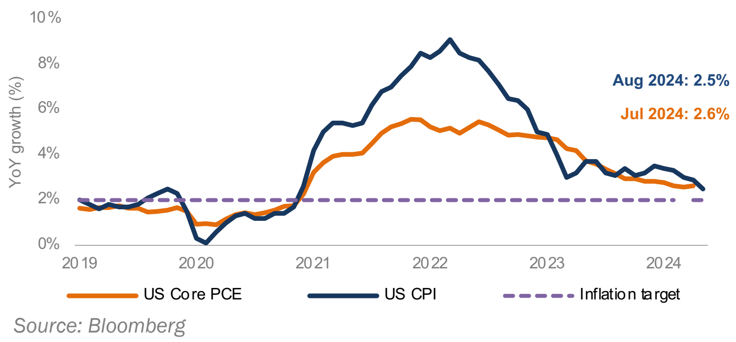
US Economic Data

The Fed's preferred inflation measure, the US Core Personal Consumption Expenditure (Core PCE) Price Index, accelerated at 2.6% year-on-year (YoY) in July for the third straight month since May. The latest data print lowered the year-to-date (YTD) inflation to 2.7%. Services inflation remains as the main contributor of Core CPE with a 2.5-percentage-point (ppt) share of the total core PCE YoY growth. On a month-on-month (MoM) basis, core PCE also increased by 0.2%, the same pace as in the preceding month.

Meanwhile, headline Consumer Price Index (CPI) decelerated further to 2.5% YoY in August from 2.9% in July, bringing down the YTD inflation rate to 3.1%. Shelter prices remain sticky and continue to drive inflation, with a majority share of 1.8 ppts out of the total 2.5%. Similar with Core PCE, it increased moderately at 0.2% MoM.

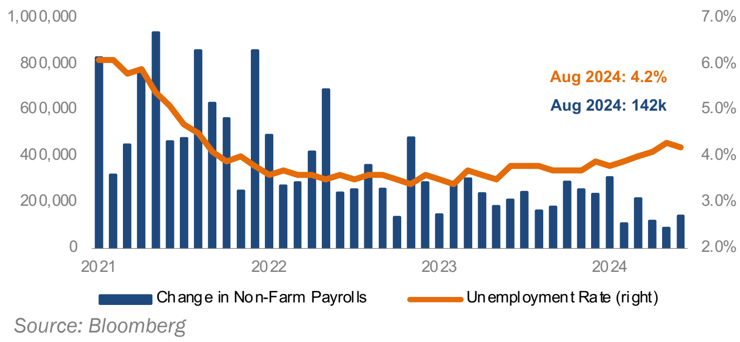
The job market remains strong given the moderation of job gains. The latest Non-Farm Payrolls data show an increase of 142,000 in August 2024, higher than the consensus estimate of 165,000 for the month. Although the US unemployment rate increased in the past months, it remains low at 4.2% in August.

US Inflation
2017=100



Source: Bloomberg

US Labor Market
Non-Farm Payrolls



Source: Bloomberg

METRO RESEARCH'S TAKE

Given the "dovish" 50-bp cut by the Fed, Metrobank Research revises its forecast for the Fed Funds Rate (FFR). We now expect a total of 100 bps worth of Fed cuts for FY 2024 and another 100 bps for FY 2025. The recent 50-bp cut will be followed by 25-bp cuts at each of the remaining FOMC meetings (November and December). This should bring the target FFR range to 4.25%-4.50% by year-end and 3.25% - 3.50% by end-2025.

On the domestic front, the Fed move opens the door for a 25-bp cut in October by the Bangko Sentral ng Pilipinas (BSP). Metrobank Research maintains its view that the BSP will reduce its policy rate by a total of 75 bps in 2024, translating to a 25-bp cut each in both the October and December meetings. This would bring the BSP's target reverse repurchase (RRP) rate down to 5.75% by year-end. The interest rate differential between the BSP and the US Fed would settle at 125 bps. Previously, BSP Governor Eli Remolona Jr. signaled a modest 50 bps of cumulative cuts for the year. A BSP pause in October suggests the BSP would only get a chance to adjust policy rates after two more projected Fed rate cuts. For 2025, Metrobank Research forecasts a total of 100 bps by the BSP, which shall bring policy rates down to 4.75%, maintaining the projected 125 bps differential.

Given the weak dollar environment which recently saw the USD/PHP spot rate dropping to the 55-level, Metrobank Research revises its year-end USD/PHP forecast to 55.3 for 2024 and 54.5 for 2025. These forecasts also take into consideration the expected net dollar inflows from remittances in 4Q which would be partially offset by a projected wider trade deficit.

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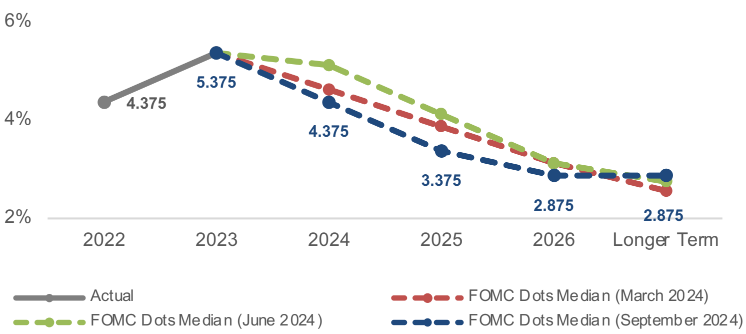
POLICY RATE VIEWS

US Federal Reserve's Summary of Economic Projections

Fed's Economic Projections (in %)	as of June 2024				as of September 2024			
	2024	2025	2026	Longer run	2024	2025	2026	Longer run
Real GDP	2.1	2.0	2.0	1.8	2.0	2.0	2.0	1.8
Unemployment Rate	4.0	4.2	4.1	4.2	4.0	4.4	4.3	4.2
PCE Inflation	2.6	2.3	2.0	2.0	2.3	2.1	2.0	2.0
Core PCE Inflation	2.8	2.3	2.0		2.6	2.2	2.0	

Source: US Federal Reserve

Fed Dot Plot



Source: US Federal Reserve

All in a day's work: Fed shifts concerns to jobs

The Fed's focus has now shifted to the labor market with inflation easing in the US. The accompanying Summary of Economic Projections (SEP) of the Fed shows a downward revision to its inflation projection, indicating a faster pace to move to its 2% target. However, it revised upward its unemployment rate projection this year and in the medium-term.

Both Personal Consumption Expenditure (PCE) and Core PCE are projected to settle lower this year at 2.3% and 2.6%, and next year at 2.1% and 2.2%, respectively.

Meanwhile, Fed officials see unemployment risk tilted more on the upside. The latest projection indicates an even higher unemployment rate projection in 2025 and 2026 at 4.4% and 4.3%, respectively. This is higher than previous projections in March at 4.2% and 4.1%, respectively, and even higher than its March projection of 4.1% and 4.0%, respectively.

Dippin (Fed) Dots

The FOMC voted 11 to 1 for a 50-bp cut in their last meeting, with only one member favoring a smaller 25-bp cut, to support economic growth in the US and achieve a "soft landing".

The so called "dot plot" of the Fed changed drastically from the last SEP in March, which only indicated a total of 25 bps in cuts for the year. The latest median projection now points policy rate towards an upper bound of 4.50% in 2024 and 3.50% in 2025, implying the possibility of a total of 200 bps worth of cuts in two years.

However, the September SEP also revealed that the FOMC is projecting a higher terminal Fed Funds rate at 2.875% in the longer term, compared to the previous projection of 2.75% last March.