



CIO Memo

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Key takeaways

- The Federal Open Market Committee (FOMC) announced for the fourth consecutive time, its decision to leave rates unchanged at their current level of 5.25% - 5.50%.
- The Fed noted that even while economic indicators point towards an economy coming into greater balance, moderation may not be solid enough yet to warrant an imminent cut in rates.
- Markets were widely anticipating a hold in rates with greater expectation that a cut would be delivered in March. However, today's meeting suggests that the FOMC are willing to remain patient before making its first move.

1. What happened?

Today the FOMC announced its decision to keep the Fed Funds Rate at its current level of 5.25% - 5.50%. The decision to hold this month was accompanied by an FOMC statement indicating that the Fed is not yet ready to cut rates until there is greater 'confidence' that inflation is moving 'sustainably' towards their 2% target. Currently, the Fed may still be more focused on maintaining rates at their current level rather than stimulating the economy.

In the official policy statement, the FOMC acknowledged that even if inflation has eased over the past year with job growth moderating, the economy has still been 'expanding at a solid pace' and the labor market continues to retain a strong foothold. Indicating that a continued decline in inflation will be necessary for the Fed to entertain a rate cut soon.

The Fed's decision comes at a time when GDP expanded this past quarter, inflation is moderating but slowly and Nonfarm Payrolls numbers from January were stronger than expected. During the press conference, Chairman Jerome Powell emphasized that even if 'supply and demand is at a better balance', the economic outlook is 'uncertain', and that the Fed would need to continue to monitor economic data to make a sound decision on the timing of the rate cut. The Fed remains committed to its goal of striking a balance between its dual mandates of maximum employment and price stability.

Chairman Powell also mentioned that the Fed is currently in 'risk management mode' and any surprises to future economic data releases – i.e., if Nonfarm Payroll numbers come in weaker than expected, or if inflation proves to be less sticky, an earlier cut in rates may be warranted. However, Powell noted that the economy has still not achieved the much sought after 'soft-landing' scenario and, reiterating the committee's desire for greater 'confidence', appeared to push back against the idea of cutting rates in March.

FOMC: Looking for confidence

2. How did markets react?

Prior to FOMC's rate decisions today, markets were trading lower as it digested the losses posted by a U.S. regional bank, potentially being the first regional bank being adversely affected by the sustained high interest rate environment. Markets did not react positively to the rates decision today – even though the Fed kept its rates steady as expected, Chairman Powell's comments around the path of future rate cuts were more conservative, pushing the start of rate cuts later into the year.

At the time of writing, both the S&P 500 and NASDAQ were trading in negative territory, reaching -1.61% and -2.23% respectively. Sizeable moves were seen in bond markets with 2-Year Treasury yields falling to 4.20% and 10-Year Treasury yields reaching 3.92%. The probability of a rate cut in March also moved lower to 36.8%.

3. What does it mean for investors?

The latest Fed meeting continues the trend of previous months as the FOMC left the Federal Funds Rate unchanged. More significant to markets has been the changes in tone from both the official statement as well as Chairman Powell's own press conference comments. In December, markets rallied following a more dovish stance taken by Powell with expectations for a March rate cut reaching a 76% probability.

Since then, expectations have certainly tempered as the labor market and economic data continued to lean towards a patient stance, albeit as inflation continues to move lower. Today, the Federal Reserve appeared to push back further to this expectation with changes to the FOMC statement that acknowledges an overall healthier picture for the economy, but that a March rate cut is not a guarantee.

With what is a larger number of changes to the FOMC statement than usual, it appears that the Federal Reserve are more comfortable with its dovish stance, engaging more openly about cutting rates, but are clearly keen to reiterate to markets that the decision to cut rates will be taken when the FOMC are confident that inflation is fully moving in the right direction.

The FOMC will hope that such confidence can be reached with the release of key data points over the coming weeks. The latest Nonfarm Payrolls (February 2nd) and next week's CPI print (February 9th) will again be closely monitored, as wage growth and services inflation continue to remain elevated.

Following the decision to keep rates unchanged, Chairman Powell reiterated that while there is greater confidence in achieving a soft landing, the Fed is yet to be fully convinced that a rate cut is imminent.



Glossary

The [Fed funds rate](#) is the interest rate at which depository institutions lend overnight to other depository institutions.

The [Federal Reserve \(Fed\)](#) is the central bank of the United States. Its [Federal Open Market Committee \(FOMC\)](#) meets to determine interest rate policy.

Four times a year, the Federal Reserve releases a [Summary of Economic Projections \(SEP\)](#) for GDP growth, the unemployment rate, inflation, and the appropriate policy interest rates.

The [FOMC Dot Plot](#) is comprised typically of 19 dots: seven members of the Board of Governors of the Federal Reserve System and presidents of the 12 regional banks. Each is asked to indicate where they believe the Federal Funds rate should be in the future.

The [Personal Consumption Expenditure \(PCE\)](#) is a price index for goods and services, particularly relevant to the context of U.S. GDP

[Treasury](#)s are bonds issued by the U.S. government.

[USD](#) is the currency code for the U.S. Dollar.



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