28 July 2022

MARKET FLASHNOTE
FOMC MEETING AND FED PRESS CONFERENCE SUMMARY NOTE

The Federal Open Market Committee (FOMC) voted to raise the Fed Funds rate by 75-bps yesterday. This will being its key interest rate to a range of 2.25%- 2.50%- the highest level since 2018.

FOMC Committee Statement Key Points:

- Recent indicators of spending and production have softened – labor markets still strong with robust job gains and low unemployment levels.
- Inflation remains elevated due to supply and demand imbalances related to the pandemic, higher food and energy prices and broader price pressures.
- FOMC acknowledged that Russia's war against Ukraine has created additional upward pressure on inflation and is weighing on global growth. FOMC is attentive to inflation risks arising to the crisis.
- The Committee Statement removed reference to COVID related lockdowns in China.
- FOMC reiterated its commitment to achieve maximum employment and inflation rate at 2% in the longer run.
- The committee would continue to reduce its balance sheet holding of Treasury securities and agency debt and agency mortgage-backed securities in accordance with its plan outlined in May.
- The Committee will continue to monitor economic data and adjust its stance accordingly.

Fed Chair Powell Press Conference Key Points

- Reiterated the belief that the US market is not in recession and that the economy is performing well in many areas
- Reinforced that inflation was much too high and they want inflation to 2%. The Fed will look at both headline and core inflation.
- Powell stood by forecast that the Fed Funds rate will reach range of 3.25%-3.5% by end of 2022 and 50-bps more in 2023.
- The balance sheet runoff would continue at caps of USD 30 bn and USD 17.5 bn per month for US treasuries and mortgage-backed securities (MBS), before doubling to USD 60 bn and USD 35 bn for MBS starting in September.

Our View

- Stock markets reacted positively during the press conference with the NASDAQ rising by ~4%, signaling that the market believes a more dovish / neutral stance will be followed by the Fed in its future interest rate hikes.
- If the Fed sticks by its forecast of 3.25-3.5 by year end – this implies 50-bps increase in September and 25-bps points at each of its November and December meetings.
- The US housing market will be adversely affected by the pace of monetary tightening with average 30-year fixed mortgage already doubling to 5.5%, breaking its 2021 boom cycle and US housing sales have already tumbled.
- Consumer and business loans will also cool with higher interest rates, bringing inflation down.

Recession fears are not ruled out yet- with Bank of America forecasting a mild recession this year and Goldman Sachs estimating 50-50 likelihood of recession within two years.