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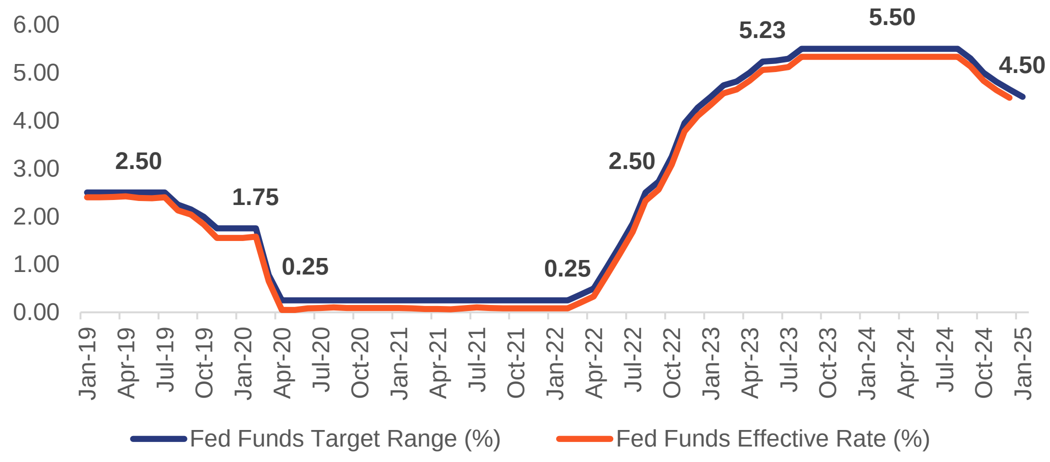
31 JANUARY 2025

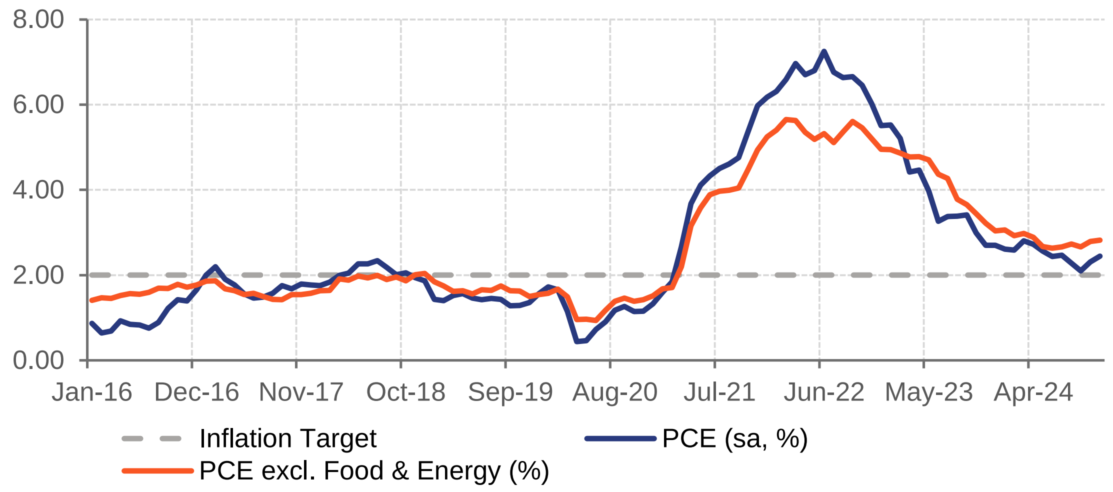
Monetary Policy Watch: Fed on a pause

Federal Funds Rate (%)



Source: The Federal Reserve Bank of St. Louis, BMMB Economics

Personal Consumption Expenditures (PCE) Price Index(%)



Source: Bloomberg, BMMB Economics

In line with our expectation, the Fed decided to hold rates steady at 4**.25%–4.50%**, reflecting a cautious yet steady-handed approach amid evolving economic conditions. While acknowledging notable progress on inflation, the Fed emphasized that price pressures remain too high, and a sustained decline toward the 2% target is required before policy easing is considered. The central bank maintained a moderate growth outlook, highlighting resilient labor market conditions with strong job gains and low unemployment, though signs of softer consumer spending have begun to emerge.

The Fed also reiterated their data-dependent approach, making it clear that future policy adjustments will hinge on incoming economic indicators, inflation expectations, and financial market developments. The Fed remains prepared to act if risks to its dual mandate of price stability and maximum employment emerge, signaling a carefully calibrated stance that aims to balance economic growth while keeping inflation in check. Markets, which had initially priced in an earlier rate cut, are now adjusting their expectations toward a mid-2025 timeline, with attention shifting to upcoming labor market and inflation figures for further policy cues.

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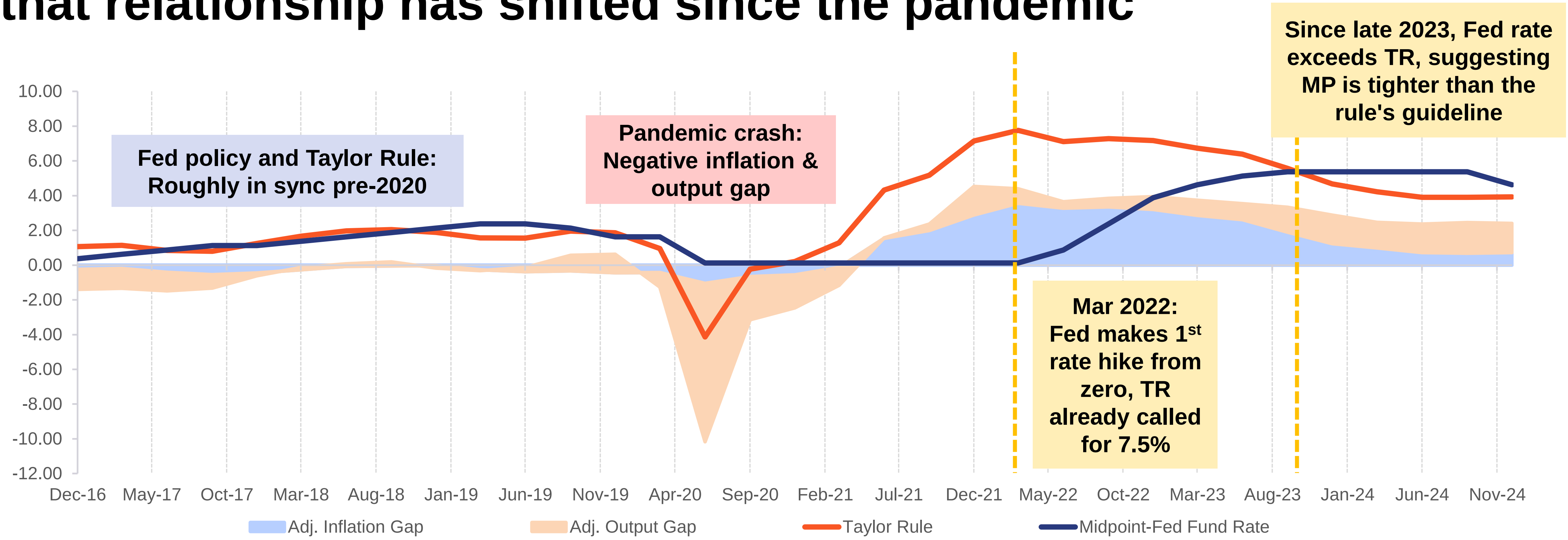
The Fed's key rate used to largely align with the Taylor Rule*, but that relationship has shifted since the pandemic



Source: CEIC, BMMB Economics

* Taylor Rule (TR) is a guideline for central banks to set interest rates based on two key economic factors: inflation and the output gap (the difference between actual economic output and its potential). It suggests that when inflation rises above the central bank's target, or when the economy is overheating (positive output gap), interest rates should be increased to cool things down. Conversely, when inflation is below target or the economy is underperforming (negative output gap), interest rates should be lowered to stimulate growth, helping maintain stable prices and full employment.

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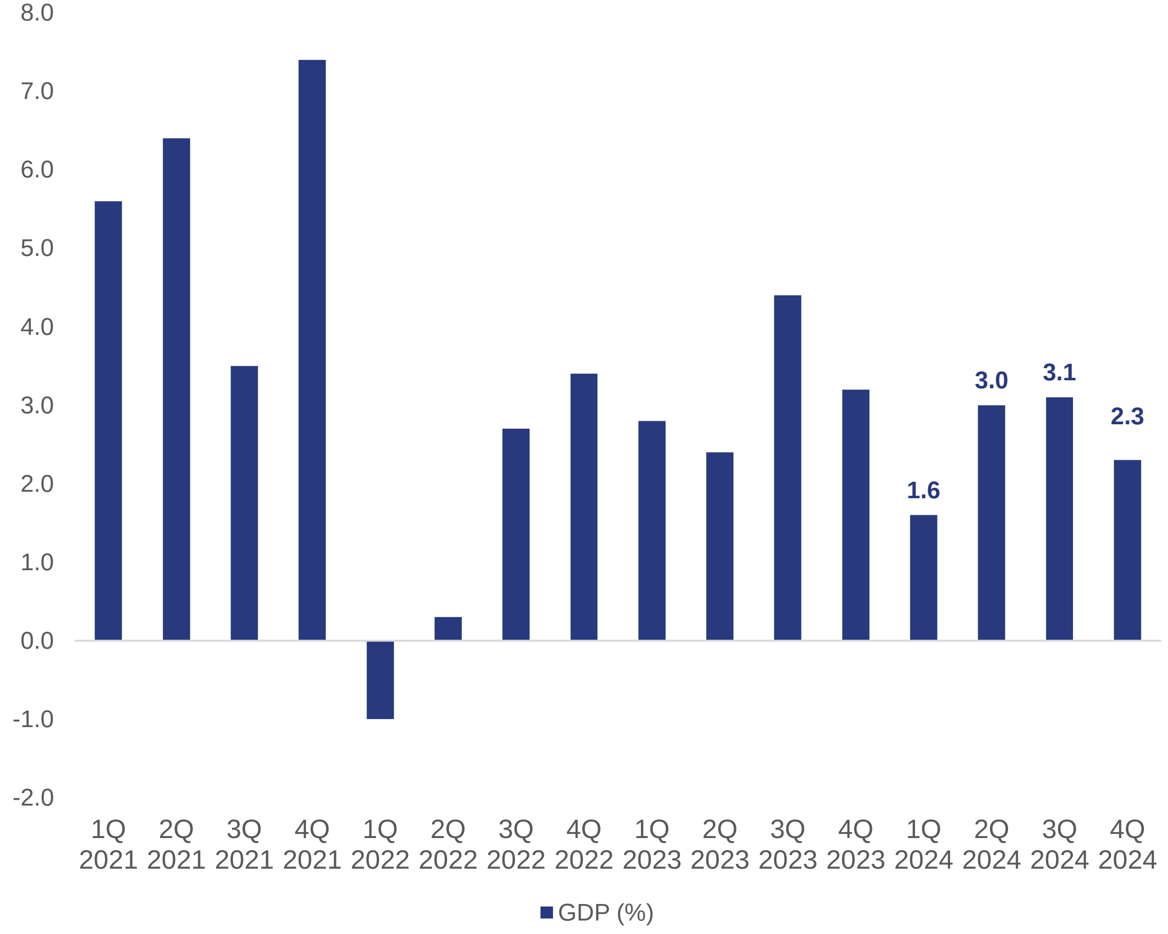
US GDP grew at a 2.3% pace in 4Q24, falling short of expectation

Real GDP, % q-o-q annualised



Source: US Bureau of Economic Analysis (BEA)

- The US economy displayed a moderate slowdown in the 4Q2024, with real GDP **growth decelerating to an annualized rate of 2.3%**, falling short of markets expectation of 2.5%. The growth in the fourth quarter primarily reflected increases in consumer spending and government spending that were partly offset by a decrease in investment.

- For the whole year 2024, the U.S. economy **expanded by 2.8%** in 2024, a slight moderation from the 2.9% growth in 2023, with consumer spending, investment, government expenditure, and exports contributing to this annual increase.

- Looking ahead, we anticipate the US economy to **sustain a modest growth trajectory** in the near term, though emerging headwinds from softer labor market conditions and tight financial conditions are likely to weigh on consumer spending and business activity. While the unemployment rate is expected to remain relatively stable in the near term, a moderation in wage growth could pose downside risks to household income. That said, we maintain our expectation that the Fed will deliver two additional rate cuts in 2025 which would bring the **Fed Fund Rate to 4.00% by end of the year.** This is contingent on further progress toward its inflation target and a gradual cooling in economic activity.

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Appendix: FOMC statement

Recent indicators suggest that economic activity has continued to expand at a solid pace. The unemployment rate has stabilized at a low level in recent months, and labor market conditions remain solid. Inflation remains somewhat elevated.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. The Committee judges that the risks to achieving its employment and inflation goals are roughly in balance. The economic outlook is uncertain, and the Committee is attentive to the risks to both sides of its dual mandate.

In support of its goals, the Committee decided to maintain the target range for the federal funds rate at 4-1/4 to 4-1/2 percent. In considering the extent and timing of additional adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. The Committee will continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities. The Committee is strongly committed to supporting maximum employment and returning inflation to its 2 percent objective.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

Voting for the monetary policy action were Jerome H. Powell, Chair; John C. Williams, Vice Chair; Michael S. Barr; Michelle W. Bowman; Susan M. Collins; Lisa D. Cook; Austan D. Goolsbee; Philip N. Jefferson; Adriana D. Kugler; Alberto G. Musalem; Jeffrey R. Schmid; and Christopher J. Waller.

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Appendix: US Quarterly GDP q-o-q seasonally adjusted annualized rate

Line		2019				2020				2021				2022				2023				2024			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
1	**Gross domestic product**	**2.5**	**3.4**	**4.8**	**2.8**	**-5.5**	**-28.1**	**35.2**	**4.4**	**5.6**	**6.4**	**3.5**	**7.4**	**-1.0**	**0.3**	**2.7**	**3.4**	**2.8**	**2.4**	**4.4**	**3.2**	**1.6**	**3.0**	**3.1**	**2.3**
2	**Personal consumption expenditures**	**0.6**	**3.5**	**4.6**	**2.7**	**-6.6**	**-30.6**	**41.2**	**5.8**	**9.5**	**14.1**	**3.1**	**4.4**	**1.0**	**2.6**	**1.5**	**1.2**	**4.9**	**1.0**	**2.5**	**3.5**	**1.9**	**2.8**	**3.7**	**4.2**
3	Goods	1.1	7.1	5.8	1.3	-2.3	-9.1	51.8	3.1	17.9	14.4	-9.6	4.6	-1.7	-1.5	-2.3	-0.7	7.4	-0.3	3.5	3.4	-1.2	3.0	5.6	6.6
4	Durable goods	-3.5	12.2	9.8	3.3	-17.2	-1.6	100.8	4.5	31.0	14.7	-24.8	8.6	0.1	-2.2	-1.9	-2.0	17.1	-0.3	4.2	2.9	-1.8	5.5	7.6	12.1
5	Nondurable goods	3.5	4.6	3.9	0.4	6.0	-12.5	31.0	2.3	10.9	14.2	0.4	2.5	-2.7	-1.2	-2.5	0.1	2.5	-0.4	3.1	3.6	-0.8	1.7	4.6	3.8
6	Services	0.4	1.8	4.0	3.2	-8.5	-39.1	36.1	7.1	5.4	13.9	10.4	4.3	2.4	4.7	3.5	2.2	3.8	1.6	2.1	3.5	3.4	2.7	2.8	3.1
7	**Gross private domestic investment**	**3.3**	**3.7**	**3.2**	**-5.1**	**-9.9**	**-45.1**	**97.1**	**13.0**	**-2.4**	**-6.4**	**16.3**	**28.3**	**7.4**	**-8.5**	**-5.7**	**5.8**	**-8.9**	**8.0**	**10.1**	**0.7**	**3.6**	**8.3**	**0.8**	**-5.6**
8	Fixed investment	1.1	7.6	4.3	-1.1	-3.0	-27.8	28.7	16.0	9.4	5.5	-2.1	2.9	8.5	2.0	-1.8	-1.9	3.1	8.6	2.6	3.5	6.5	2.3	2.1	-0.6
9	Nonresidential	2.7	7.8	3.9	-1.8	-7.4	-28.5	18.7	11.1	9.6	8.9	-1.8	3.4	13.6	7.3	7.7	5.7	5.3	9.9	1.1	3.8	4.5	3.9	4.0	-2.2
10	Structures	1.5	13.5	16.8	-6.6	-4.6	-39.1	-6.5	1.8	8.8	0.6	-3.8	-9.5	10.9	8.8	9.2	9.8	14.9	16.4	1.7	6.5	6.3	0.2	-5.0	-1.1
11	Equipment	2.2	4.1	-5.8	-8.7	-20.1	-38.3	50.4	17.3	5.3	8.7	-10.6	1.5	16.4	1.1	6.6	1.1	0.9	12.5	-1.1	0.7	0.3	9.8	10.8	-7.8
12	Intellectual property products	4.2	8.9	8.1	10.1	6.0	-9.5	7.7	10.3	14.3	13.8	8.6	12.4	12.6	12.7	8.0	7.9	4.5	3.9	2.8	5.2	7.5	0.7	3.1	2.6
13	Residential	-4.4	7.0	5.9	1.3	14.1	-25.7	66.2	31.0	8.7	-3.7	-3.4	1.2	-4.5	-11.6	-25.2	-22.8	-4.3	4.5	7.7	2.5	13.7	-2.8	-4.3	5.3
14	Change in private inventories	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---
15	**Net exports of goods and services**	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---
16	Exports	3.8	-2.0	0.1	2.5	-16.1	-61.3	60.2	26.8	0.3	3.2	0.9	25.5	-4.6	12.7	14.5	-1.1	2.0	-4.8	4.9	6.2	1.9	1.0	9.6	-0.8
17	Goods	3.6	-7.4	3.2	1.8	-5.2	-66.7	105.3	28.5	-1.2	1.2	-2.7	27.6	-9.4	10.9	20.3	-5.4	5.3	-10.9	7.5	5.3	-0.2	0.9	10.3	-5.0
18	Services	4.3	8.9	-5.4	3.7	-33.3	-49.2	0.8	22.8	3.3	7.4	8.9	21.1	6.9	16.8	2.6	8.7	-4.5	8.8	0.0	8.0	6.1	1.2	8.4	7.2
19	Imports	-0.2	2.2	-1.7	-7.3	-13.7	-52.8	85.7	32.3	8.3	8.3	8.6	20.8	13.4	5.9	-5.4	-4.5	-0.8	-3.1	4.7	4.2	6.1	7.6	10.7	-0.8
20	Goods	-2.1	2.0	-1.5	-8.4	-10.1	-48.6	100.9	31.3	8.0	5.3	0.9	21.7	13.6	3.1	-8.2	-4.0	0.1	-5.0	5.1	1.8	6.5	8.4	10.7	-4.0
21	Services	8.5	3.4	-2.8	-2.6	-27.8	-67.7	25.1	37.6	9.9	25.5	55.3	16.6	12.4	20.4	8.1	-6.9	-4.8	5.0	2.6	14.8	4.8	4.3	11.0	12.8
22	**Government consumption expenditures and gross investment**	**5.6**	**5.5**	**4.6**	**3.3**	**4.4**	**8.9**	**-6.0**	**-1.5**	**5.2**	**-4.2**	**-1.5**	**-0.3**	**-3.4**	**-1.5**	**1.6**	**5.4**	**5.1**	**2.9**	**5.7**	**3.6**	**1.8**	**3.1**	**5.1**	**2.5**
23	Federal	4.4	4.1	5.1	2.2	4.2	32.9	-12.1	0.1	17.2	-8.0	-7.5	3.1	-8.5	-3.3	-0.4	9.0	4.6	-1.1	5.3	-0.3	-0.4	4.3	8.9	3.2
24	National defense	9.7	-0.9	6.2	2.5	2.5	2.1	-0.1	12.9	-7.9	-2.8	-4.6	-3.7	-11.2	2.0	-2.9	7.6	4.9	0.8	6.7	-1.3	-2.5	6.4	13.9	3.3
25	Nondefense	-2.9	12.0	3.5	1.8	6.8	90.3	-25.6	-15.4	63.0	-14.3	-11.3	13.0	-5.0	-9.7	2.9	10.8	4.3	-3.5	3.4	0.9	2.6	1.5	2.6	3.1
26	State and local	6.4	6.4	4.4	3.9	4.5	-3.6	-2.0	-2.5	-1.6	-1.8	2.3	-2.3	-0.1	-0.4	2.7	3.4	5.3	5.4	5.9	6.1	3.1	2.3	2.9	2.0

Source: US Bureau of Economic Analysis (BEA)