MARKET SIGHT LINES

The Federal Reserve Sees Improving Inflation, Yet Signals Higher Rates Through 2024

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Interest rates have been higher for longer, given the Federal Reserve's (Fed's) restrictive monetary policy designed to bring down inflation. The Fed held its June meeting this week, signaling that inflation has improved some, but more improvement is needed. In this week's Sight|Lines, we unpack the results of the Fed's June 2024 meeting and the recently released Summary of Economic Projections (SEP).

THE TAKEAWAY: SOME INFLATION PROGRESS, BUT MORE NEEDED

The Fed likes the improved inflation but kept rates steady and now projects fewer cuts this year. In summary:

- The central bank left its current restrictive policy unchanged.
- The Fed statement acknowledged some inflation improvement.
- The statement also reinforced that the Fed will remain data dependent.
- The SEP summarizes the economic projections of individual Fed officials.
- The median projection for GDP still implies strong positive growth going forward.
- The Fed expects unemployment to stay low but rise next year.
- Officials still project inflation to be above the Fed's 2% target for a while.
- The median projection for the fed funds rate rose, now signaling only one 0.25% cut this year.
- In his press conference, Fed Chair Jerome Powell offered more perspective, noting that risk factors are in better balance.
- Powell also signaled the Fed believes its current policy will be sufficiently restrictive.

IN-DEPTH: SOME INFLATION PROGRESS, BUT MORE NEEDED

The Fed acknowledged some inflation improvement but left its policy unchanged, keeping the fed funds rate steady and signaling the possibility of fewer cuts later this year. Going deeper:

- The central bank left its current policy, which is restrictive, unchanged:
  - The fed funds rate remains at 5.25%-5.50%.
  - The Fed will continue to slowly reduce its security holdings.
- The Fed statement is carefully crafted, so changes from previous statements are important:
  - This statement introduced the idea of "modest further progress" on inflation.
- The statement also reinforced that the Fed will remain data dependent:
  - "In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook."
- The SEP, which is published four times per year, captures and summarizes the economic projections of individual Fed officials.
- The projections still imply strong positive GDP growth going forward:
  - Median GDP growth is projected at 2.1% in 2024 and 2.0% in 2025, unchanged from March.
- Unemployment is projected to stay low, but rise next year:
  - The median is 4.0% in 2024 and 4.2% in 2025, with the latter up 0.1% since March.
- Officials still project inflation to take some time to cool, reaching the 2% target in 2026:
  - PCE Inflation is projected at 2.6% for 2024 and 2.3% in 2025, up modestly from March.
- The median projection for the fed funds rate rose, now signaling only one 0.25% cut this year.
  - The median fed funds rate projection for year-end 2024 rose from 4.6% in March to 5.1% in this SEP.
- In his press conference, Chair Powell offered more perspective:
  - Powell noted that risk factors – the interplay of labor, inflation, and the economy – are in better balance.
  - He also said, "I think the evidence is pretty clear. This policy is restrictive and is having the effect we would hope for."

CONCLUSION

Inflation has been elevated in recent years, resulting in a Fed policy that has been, and continues to be, highly restrictive. The Fed has kept the fed funds rate higher for longer and is signaling it will continue to do so for the remainder of 2024, despite some modest signs of improving inflation. Market rates tend to adjust to Fed policy, so this Fed meeting result reinforces that we should expect to see market interest rates higher for longer from here.

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