

Initial Thoughts on FOMC Decision

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Door Left Open for Further Rate Hikes

Neutral Stance on Possibility of Another Rate Hike in September

- Today, the Federal Open Market Committee (FOMC) unanimously decided to increase the policy interest rate—the target range for the federal funds rate—from 5.00%-5.25% to 5.25%-5.50%. Being accompanied by an augmented level of quantitative tightening, allowing redemption of securities held at a faster pace in September of last year, the Federal Reserve's (the "Fed") stance on overall monetary policy remained tight.
- Last month, the Fed said it could raise interest rates at least twice for the remainder of this year, reinforcing its commitment to curbing inflation. Since then, the economic indicators have been firm on employment, and the inflation rate has eased to a monthly rate of change comparable to the target of 2%. In other words, an economic recession is not expected in the near future. Anxiety about the banking system has generally eased, though the problems have not been fully resolved.
- The economic assessment shown in today's statement has not changed from the previous time, maintaining that employment is robust and prices are elevated. More importantly, the evaluation regarding the pace of expansion of business activities was slightly upwardly revised from "modest" in June to "moderate" this time. Leaving a positive evaluation in the statement reflects the intention to shrug off the market's calls for a policy pivot in the near future, before the FOMC gains confidence on containing inflation risks.
- The main focus for today's meeting was to what extent the FOMC would show a willingness to raise interest rates further at the next and subsequent meetings. Given that there were no conspicuous downward revisions to the economic assessment, and that phrases such as "the Committee remains highly attentive to inflation risks" remained, there seems a fair chance that the Fed will continue its rate hikes.
- The first question at the post-meeting press conference was precisely on the possibility of a rate hike in September. Fed Chair Jerome Powell stressed that policy decisions should be made at each meeting rather than looking ahead to the next few meetings, providing the audience a seemingly neutral answer.

Jackson Hole Symposium May Provide Clues on Future Policy

- Compared to the Fed chair's remark last month that "at least two rate hikes would be appropriate this year," these comments sounded like a somewhat more conservative statement about the possibility of further interest-rate hikes. However, it rather implies the Fed's intention to wait and see the cumulative impact of its monetary tightening on business activities. In addition, the period until the next FOMC meeting in September is relatively long, with two months' worth of employment statistics and price indicators to be released, and from August 24 to 26, officials from major central banks and academics will discuss policies when they meet at the Jackson Hole Economic Policy Symposium.
- If the inflation indicators for the next two months display a steady slowdown, even if the policy interest rate remains unchanged at 5.25%-5.50%, the real interest rate (nominal policy interest rate – inflation rate) will rise and monetary policy will be tightened further. In the meantime, if the Fed gains confidence that the slowdown in inflation is not temporary and that upside risks to prices have eased, the Fed will make a formal statement about it and decide how long it will continue to tighten policy. The current situation is still one step short of that.
- FOMC members appear to be divided on the cumulative effects of past tightening policies. Doves weighed heavily on the pessimistic view that further interest-rate hikes would overwhelm the financial system, which could depress final demand more than the Fed expects. On the other hand, long-lasting discussions among policy members on topics such as 1) the structure of the economy has changed dramatically over the past few years; 2) the fact that fiscal policy cannot be expected to be tightened for the time being, monetary policy will be given more weight to curb inflation; and 3) some arguments that the neutral policy rate can be somewhat higher than the Fed assumes at 2.5% could all reinforce the hawks' preference to tighten the policy more and longer.
- Thus, depending on the economic indicators for the next two months and the message conveyed at the Jackson Hole symposium, the pros and cons of another interest-rate hike and how long the high policy rate should be maintained are still subject to change.

SMBC Economy and Rates Forecast

		2022			2023				2024				2021	2022	2023	2024
		Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
U.S.	Real GDP (saar)	-0.6	3.2	2.6	1.3	1.5	-0.8	0.6	0.9	1.4	1.8	2.2	5.9	2.2	1.4	1.0
	Inflation rate (YoY)	5.0	4.9	4.8	4.8	4.6	4.2	3.9	3.2	2.8	2.5	2.2	3.3	5.0	4.4	2.7
	Jobless rate	3.6	3.6	3.6	3.5	3.5	3.7	4.3	4.6	4.7	4.7	4.6	5.4	3.7	3.7	4.7
Euro area	Real GDP (qoq)	0.8	0.4	-0.1	-0.1	0.3	0.2	0.1	0.1	0.4	0.3	0.3	5.4	3.5	0.6	0.9
	Inflation rate (YoY)	8.0	9.3	10.0	8.0	6.2	4.8	3.2	3.1	2.9	2.7	2.5	2.6	8.4	5.6	2.8
	Jobless rate	6.7	6.7	6.7	6.6	6.6	6.6	6.7	6.8	6.8	6.9	6.9	7.7	6.7	6.6	6.9
Japan	Real GDP (saar)	5.6	-1.5	0.4	2.7	1.7	1.0	0.9	0.9	0.8	0.8	0.7	2.3	1.1	1.0	0.9
	Inflation rate (YoY)	2.1	2.7	3.8	3.5	3.3	2.8	2.3	2.9	2.7	2.6	2.2	-0.2	2.6	3.0	2.6
	Jobless rate	2.6	2.5	2.5	2.6	2.5	2.4	2.4	2.3	2.3	2.3	2.3	2.8	2.6	2.4	2.3
China	Real GDP (YoY)	0.4	3.9	2.9	4.5	8.4	5.7	6.3	5.4	5.2	5.1	5.0	8.4	3.0	6.3	5.2
	Inflation rate (YoY)	2.2	2.8	1.8	1.3	1.6	1.4	1.5	1.6	1.9	2.0	2.0	0.8	1.7	1.5	1.9
	Jobless rate	5.8	5.4	5.6	5.5	5.4	5.1	4.9	4.9	4.9	5.0	5.0	5.1	5.1	5.2	5.0

Rates		2022	2023				2024				2022	2023	2024
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
U.S.	FF target range	4.25	4.75	5.00	5.25	5.25	5.00	4.75	4.50	4.25	4.25	5.25	4.25
		~	~	~	~	~	~	~	~	~	~	~	~
	2yr UST	4.50	5.00	5.25	5.50	5.50	5.25	5.00	4.75	4.50	4.50	5.50	4.50
	10yr UST	3.43	4.03	4.90	4.20	4.00	3.80	3.60	3.40	3.20	3.20	4.00	3.20
Germany	ECB refi rate	2.50	3.50	4.00	4.25	4.25	4.25	4.25	4.00	3.75	2.50	4.25	3.75
	ECB depo rate	2.00	3.00	3.50	3.75	3.75	3.75	3.75	3.50	3.25	2.00	3.50	3.25
	2yr Schatz	2.50	2.68	3.20	3.20	3.00	2.80	2.50	2.40	2.30	2.50	3.00	2.30
	10yr Bunds	2.20	2.29	2.39	2.30	2.30	2.30	2.20	2.10	2.10	2.20	2.30	2.10
Japan	IOER	-0.10	-0.10	-0.10	-0.10	-0.10	0.10	0.10	0.10	0.10	-0.10	-0.10	0.10
	2yr JGB	0.04	-0.06	-0.07	0.10	0.15	0.20	0.30	0.30	0.30	0.04	0.15	0.30
	10yr JGB	0.42	0.35	0.40	0.75	0.75	0.75	0.90	0.90	0.90	0.42	0.75	0.90
China	Policy rate	2.75	2.75	2.65	2.55	2.55	2.55	2.55	2.55	2.55	2.75	2.55	2.55
	2yr gov bond	2.40	2.41	2.11	2.16	2.24	2.32	2.39	2.49	2.59	2.40	2.24	2.59
	10yr gov bond	2.83	2.85	2.64	2.64	2.69	2.74	2.79	2.84	2.89	2.83	2.69	2.89

Source: SMBC

SMBC FX Forecast

		2022	2023				2024				2022	2023	2024
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
USD/JPY	Range	130.58	127.23	130.64	128.00	125.00	121.00	119.00	116.00	116.00	113.47	125.00	116.00
		~ 151.95	~ 137.91	~ 145.07	~ 147.00	~ 138.00	~ 135.00	~ 133.00	~ 130.00	~ 130.00	~ 151.95	~ 147.00	~ 135.00
	End of period	133.00	132.86	144.31	137.00	133.00	130.00	128.00	126.00	123.00	131.12	133.00	123.00
EUR/USD	Range	0.9633	1.0484	1.0635	1.0300	1.0200	1.0100	1.0000	1.0100	1.0100	0.9536	1.0200	1.0000
		~ 1.0735	~ 1.1033	~ 1.1095	~ 1.1300	~ 1.1200	~ 1.1100	~ 1.1000	~ 1.1100	~ 1.1100	~ 1.1495	~ 1.1300	~ 1.1100
	End of period	1.0705	1.0839	1.0909	1.0700	1.0600	1.0500	1.0500	1.0600	1.0600	1.0705	1.0600	1.0600
USD/CAD	Range	1.3275	1.3291	1.3151	1.3000	1.3000	1.3000	1.3000	1.2800	1.2700	1.2477	1.3000	1.2700
		~ 1.3885	~ 1.3832	~ 1.3642	~ 1.4200	~ 1.4200	~ 1.4200	~ 1.4200	~ 1.4000	~ 1.3800	~ 1.3885	~ 1.4200	~ 1.4200
	End of period	1.3554	1.3516	1.3242	1.3500	1.3600	1.3500	1.3500	1.3400	1.3300	1.3554	1.3600	1.3300
CAD/JPY	Range	96.76	95.13	97.54	95.00	91.00	90.00	88.00	88.00	85.00	89.77	91.00	85.00
		~ 109.11	~ 100.59	~ 109.21	~ 108.00	~ 103.00	~ 102.00	~ 100.00	~ 100.00	~ 98.00	~ 110.06	~ 109.21	~ 102.00
	End of period	96.76	98.28	109.04	101.48	97.80	96.30	94.81	94.03	92.48	96.76	97.80	92.48
EUR/JPY	Range	138.81	138.19	143.12	144.00	136.00	131.00	128.00	126.00	123.00	124.40	136.00	123.00
		~ 148.40	~ 145.67	~ 157.92	~ 158.00	~ 150.00	~ 145.00	~ 142.00	~ 140.00	~ 137.00	~ 148.40	~ 158.00	~ 145.00
	End of period	140.41	144.01	157.44	146.59	140.98	136.50	134.40	133.56	130.38	140.41	140.98	130.38
Oil price (WTI futures)		82.64	75.99	73.58	75.00	80.00	80.00	75.00	77.00	78.00	98.74	76.37	77.50

Source: SMBC