Fed Watch

Powell doesn't think a March rate cut is likely

Javier Amador / Iván Fernández

January 31, 2024

FOMC participants need "more good data" to achieve "greater confidence" that inflation is moving sustainably down to 2%

- **The FOMC kept the fed funds rate unchanged at 5.25-5.50%, and hinted through its policy statement that the rate-cut cycle is not likely to start in March.** The policy statement had quite a few changes. The assessment about the unemployment rate (which "has remained low") and inflation (which "has eased over the past year but remains elevated") remained unchanged, but the FOMC upgraded its view about economic activity as having "been expanding at a solid pace" following the last week's above-expectations real GDP figure for 4Q23. The paragraph used to convey the uncertainty around the effects of last year's banking turmoil on financial conditions was removed, reflecting greater confidence by the FOMC around the soundness of the financial system. Additional changes to the statement suggest the Fed is moving further away from its long-held tightening bias. While the FOMC continued to stress its duty to "carefully assess [...] the evolving [and uncertain] outlook [and] the balance of risks" in "considering any adjustments to the target range for the federal funds rate," it explicitly conveyed that "the risks to achieving its employment and inflation goals are moving into better balance." More importantly, the statement brought up the issue of rate cuts, though hinting that they are not likely to begin in March (contrary to what markets were strongly expecting a few weeks ago), as the FOMC "does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent."

- **Chair Powell reinforced such a signal by explicitly stating that the FOMC was unlikely to reach a sufficient level of confidence by March to deliver its first rate cut.** During the press conference, he explained that "it [was] not that [the Fed did not] have any confidence," but in fact there was "growing confidence" among participants that inflation will move toward 2% permanently[1]. Moreover, he explained that we have had "six months of good inflation" and the FOMC was not looking for "better data," only "more good data." He clearly stated that they have confidence, but "need to see continuation of good data." He also added that he did not think that weaker growth and/or a weaker labor market was inevitably needed. Yet, probably halfway through the Q&A session, Chair Powell explicitly stated that he did not think a March rate cut was likely: "I don't think it's likely that the Committee will reach a level of confidence by the time of the March meeting [...] I don't think that's the base case." The odds of a rate cut in March moved down sharply as a consequence and, at the time of writing this report, stand at around ⅓ after hovering around 50% over the past few days.

- **Powell reinforced the meeting-by-meeting and data-dependent approach going forward, but raised the bar for a rate cut at the next meeting.** What would it take for the Fed to start to cut rates in March? Powell was clear. For the Fed to move sooner, participants will need to see either a "weaker labor market" or "very persuasive lower inflation." Given that inflation has been running on annualized terms slightly below the target for the past six months and that Powell implicitly stated that two more months of good inflation numbers were

[1] He added: "we do have confidence and [it] has been increasing, but we need greater confidence."

likely not enough for the Fed to start to slash rates, he clearly signaled that only a noticeable deterioration in the labor market will convince them to cut sooner.

- **We continue to expect the rate cut cycle to start in May. Today's meeting increased the odds of this outcome.** Yet, today's statement and some comments from Chair Powell also (implicitly) signaled that once the Fed is confident to start to cut rates it might not skip at the first meetings of the cycle. For now, we continue to expect 100 bps worth of cuts in 2024 and a further 150 bps in 2025.

DISCLAIMER

The present document does not constitute an "Investment Recommendation", as defined in Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse ("MAR"). In particular, this document does not constitute "Investment Research" nor "Marketing Material", for the purposes of article 36 of the Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive (MIFID II).

Readers should be aware that under no circumstances should they base their investment decisions on the information contained in this document. Those persons or entities offering investment products to these potential investors are legally required to provide the information needed for them to take an appropriate investment decision.

This document has been prepared by BBVA Research Department. It is provided for information purposes only and expresses data or opinions regarding the date of issue of the report, prepared by BBVA or obtained from or based on sources we consider to be reliable, and have not been independently verified by BBVA. Therefore, BBVA offers no warranty, either express or implicit, regarding its accuracy, integrity or correctness.

This document and its contents are subject to changes without prior notice depending on variables such as the economic context or market fluctuations. BBVA is not responsible for updating these contents or for giving notice of such changes.

BBVA accepts no liability for any loss, direct or indirect, that may result from the use of this document or its contents.

This document and its contents do not constitute an offer, invitation or solicitation to purchase, divest or enter into any interest in financial assets or instruments. Neither shall this document nor its contents form the basis of any contract, commitment or decision of any kind.

The content of this document is protected by intellectual property laws. Reproduction, transformation, distribution, public communication, making available, extraction, reuse, forwarding or use of any nature by any means or process is prohibited, except in cases where it is legally permitted or expressly authorised by BBVA on its website www.bbvaresearch.com.

ENQUIRIES TO:
BBVA Research: Paseo de la Reforma 510, Colonia Juárez, C.P. 06600 Mexico City, Mexico.
Tel.: +52 55 5621 3434
www.bbvaresearch.com