Economic Update

July 31, 2024

U.S. Fed puts September rate cut on the table

- The U.S. Federal Reserve held the fed funds target rate unchanged in today's policy announcement as expected, while signalling the possibility of a rate cut in its next meeting in September.
- Changes to the policy statement were marginal yet uniform in recognizing more progress made towards reaching the Fed's inflation and employment goals. In the press conference, Fed Chair Powell said explicitly that should this progress continue, "a reduction of the policy rate could be on the table, as soon as September".
- Indeed, inflation prints have surprised consecutively on the low side over the summer. On labour market, Powell's assessment was that conditions are no longer overheating after a period of normalization.
- Latest in June, the unemployment rate in the U.S. rose to 4.1% which is historically low, and the amount of excess labour demand (measured as total jobs minus the size of the labour force) has declined to 1.4 million in June, comparing to 1.3 million in early 2020 just before the pandemic.
- Moving forward, we expect the normalizing in the economy will persist - GDP growth is expected to slow over the second half of 2024 but stay positive, and the unemployment rate is expected to inch only marginally higher from this point onward.
- More importantly, we think inflation prints in the U.S. will continue to improve. That's in no small part thanks to a long-awaited decline in shelter inflation, as slowing in market rent prices gradually feed through to lower rent CPI with a lag. But price pressure has also been narrowing across other services components, increasing the likelihood that the easing will persist.

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Bottom line: Data releases over the summer suggested that the U.S. economy is broadly on track for a soft landing, in line with the Fed's expectations. GDP growth remained somewhat resilient over the first half of the year, labour markets have normalized but are still strong, and inflation has come lower. Risks for a faster/larger deterioration in labour market have gained some weight remain well balanced against risks of higher inflation. Looking forward, focus will be on the next two CPI and employment releases before September, where we expect improvements will continue. We think that will prompt a first rate cut from the Fed at its next meeting, alongside the release of the dot plot that should offer more clues on the path of interest rates beyond.