

Research US

Fed review: Hawkish 75bp – Fast hikes to continue

- **Fed hiked rates by 75bp in line with our expectations. While the updated dots now signal more aggressive hiking pace, Powell provided little in terms of new concrete guidance on future policy moves.**
- **We revise our Fed call and now expect two more 75bp hikes in the November and December meetings, which would end the hiking cycle at 4.25-4.50% by year-end**
- **The statement came across as hawkish by the market, but the move reversed course during the press conference. We stick to our forecast EUR/USD to fall to 0.95 in 12M.**

Fed hiked rates by 75bp in its September meeting as widely expected. The updated ‘dot plot’ sees Fed Funds Rate rising around 4.5%, confirming that Fed will continue hiking rates aggressively in the near-term, and in line with the recent market pricing.

Powell provided little in terms of new concrete policy signals. Fed remains data dependent, and focuses increasingly on the current economic momentum and labour markets. Labour demand remains very high in historical perspective despite the recession fears and seemingly permanent shift lower in the trend path of labour supply growth.

As Powell once again reiterated during press conference, **Fed needs to continue tightening financial conditions in order to bring economy’s aggregate demand back into equilibrium with the supply.** The overheating is the most evident in the labour markets, where the constant rise in labour costs continues to create broad-based upward pressure on consumer prices.

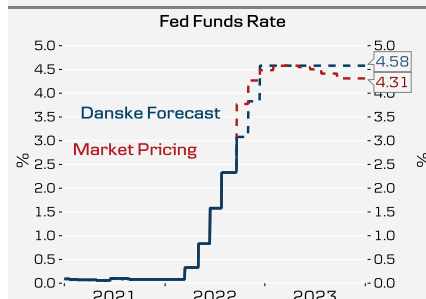
As we wrote in *Research US - Fed continues to guide US economy towards a recession*, 1 September, the recent rebound in real purchasing power points toward a modest recovery in GDP during the H2 of 2022. The near-term positive outlook means that **Fed will likely prefer continuing to frontload rate hikes in the coming meetings.** Market is looking for another 75bp in the November meeting, 50bp in December and 25bp in early 2023.

We think Fed will prefer more aggressive path, and hike 75bp in both November and December meetings. We also continue to see risks tilted towards Fed maintaining financial conditions at restrictive levels for longer. Consequently, and as Powell also acknowledged, the chances of a ‘soft landing’ have declined. Our forecast would bring the Fed Funds target rate to 4.25-4.50% by the end of the year. In terms of broader market views, we stick to our forecast for EUR/USD to fall to 0.95 in 12M.

Market reaction was modest

The statement came across as hawkish by the market, i.e. stocks lower, more curve inversion and higher USD. The market reversed course during the press conference and about erased the initial response. We note the market briefly upped the terminal rate to 4.64% in March next year, but ended around the pre-meeting pricing of 4.5%. Nevertheless, it could be an early sign the market is ready to raise the bar further for how far this hiking cycle goes.

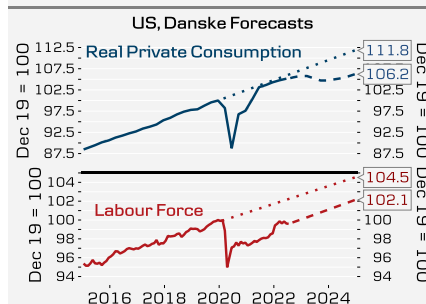
Updated Fed call: 75bp in both November and December meetings



Sources: Macrobond Financial, Refinitiv

Note: Past performance is not a reliable indicator of current or future results

Fed needs to force a modest recession to bring aggregate demand and supply back into equilibrium



Sources: Macrobond Financial, U.S. Bureau of Labor Statistics (BLS), U. S. Bureau of Economic Analysis (BEA), Danske Bank

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