

ESSENTIALS OF THE MONETARY POLICY

Federal Reserve (Fed)

Fed Announces Biggest Rate Hike since 1994

By Francis Généreux, Senior Economist

ACCORDING TO THE FED

- ▶ The Committee decided to raise the target range for the federal funds rate by 0.75%. It is now in a range of 1.50% to 1.75%.
- ▶ The Committee anticipates that ongoing increases in the target range will be appropriate. The Committee is strongly committed to returning inflation to its 2% objective.
- ▶ The Fed will continue to reduce its assets by a maximum of US\$47.5 billion per month and by a maximum of US\$95 billion per month starting in September.
- ▶ Overall economic activity appears to have picked up after edging down in the first quarter. Job gains have been robust in recent months, and the unemployment rate has remained low. Inflation remains elevated, reflecting supply and demand imbalances related to the pandemic, higher energy prices, and broader price pressures.
- ▶ The invasion of Ukraine by Russia is causing tremendous human and economic hardship. The invasion and related events are creating additional upward pressure on inflation and are weighing on global economic activity. In addition, COVID-related lockdowns in China are likely to exacerbate supply chain disruptions. The Committee is highly attentive to inflation risks.

COMMENTS

The Fed is picking up the pace of monetary tightening. After raising rates by 25 basis points in March and 50 points in May, it announced a 75-point hike today. It's the biggest increase since November 1994. Despite these recent moves, rates still aren't at restrictive levels. At 1.75%, the upper bound of the target range is still below the estimated neutral rate of 2.5%. And with inflation running north of 8%, real rates remain well in negative territory.

The Fed will therefore need to continue fighting inflation, and it said as much today. Its new dot plot shows an increase of another 175 basis points this year, but only one or two 25-point hikes next year and then a rate cut in 2024.

These quick rate hikes will affect the economy. The housing market has likely already peaked, and sales of durable goods have started to soften. The Fed downgraded its projection for real GDP growth at the end of 2022 from 2.8% to 1.7% (our call is 1.6%) and its 2023 forecast from 2.2% to 1.7%. It also expects unemployment to tick up from its current rate of 3.6% to 4.1% by the end of 2024. The Fed sees inflation remaining hot this year before slowing. It expects the 12-month change in PCE inflation to fall from 5.2% at the end of this year to 2.6% at the end of next year and 2.2% at the end of 2024.

IMPLICATIONS

Desperate times call for desperate measures, and the Fed is taking bold action to choke inflation. With Jerome Powell opening the door to another 50- or 75-point increase at the next meeting, expect more big rate hikes to come.

Schedule 2022 of Central Bank Meetings

Date	Central banks	Decision	Rate
January			
13	Bank of Korea	+25 b.p.	1.25
17	Bank of Japan	s.q.	-0.10
20	Bank of Norway	s.q.	0.50
26	Bank of Canada*	s.q.	0.25
26	Federal Reserve	s.q.	0.25
31	Reserve Bank of Australia	s.q.	0.10
February			
2	Bank of Brazil	+150 b.p.	10.75
3	European Central Bank	s.q.	0.00
3	Bank of England	+25 b.p.	0.50
10	Bank of Sweden	s.q.	0.00
10	Bank of Mexico	+50 b.p.	6.00
22	Reserve Bank of New Zealand	+25 b.p.	1.00
23	Bank of Korea	s.q.	1.25
28	Reserve Bank of Australia	s.q.	0.10
March			
2	Bank of Canada	+25 b.p.	0.50
10	European Central Bank	s.q.	0.00
16	Bank of Brazil	+100 b.p.	11.75
16	Federal Reserve	+25 b.p.	0.50
17	Bank of England	+25 b.p.	0.75
17	Bank of Japan	s.q.	-0.10
24	Bank of Norway	+25 b.p.	0.75
24	Bank of Mexico	+50 b.p.	6.50
24	Swiss National Bank	s.q.	-0.75
April			
5	Reserve Bank of Australia	s.q.	0.10
12	Reserve Bank of New Zealand	+50 b.p.	1.50
13	Bank of Korea	+25 b.p.	1.50
13	Bank of Canada*	+50 b.p.	1.00
14	European Central Bank	s.q.	0.00
27	Bank of Japan	s.q.	-0.10
28	Bank of Sweden	+25 b.p.	0.25
May			
3	Reserve Bank of Australia	+25 b.p.	0.35
4	Bank of Brazil	+100 b.p.	12.75
4	Federal Reserve	+50 b.p.	1.00
5	Bank of England	+25 b.p.	1.00
5	Bank of Norway	s.q.	0.75
12	Bank of Mexico	+50 b.p.	7.00
24	Reserve Bank of New Zealand	+50 b.p.	2.00
25	Bank of Korea	+25 b.p.	1.75
June			
1	Bank of Canada	+50 b.p.	1.50
7	Reserve Bank of Australia	+50 b.p.	0.85
9	European Central Bank	s.q.	0.00
15	Federal Reserve	+75 b.p.	1.75
15	Bank of Brazil		
16	Bank of England		
16	Bank of Japan		
16	Swiss National Bank		
23	Bank of Norway		
23	Bank of Mexico		
30	Bank of Sweden		

Date	Central banks	Decision	Rate
July			
5	Reserve Bank of Australia		
12	Reserve Bank of New Zealand		
13	Bank of Korea		
13	Bank of Canada*		
20	Bank of Japan		
21	European Central Bank		
27	Federal Reserve		
August			
2	Reserve Bank of Australia		
3	Bank of Brazil		
4	Bank of England		
11	Bank of Mexico		
16	Reserve Bank of New Zealand		
18	Bank of Norway		
24	Bank of Korea		
September			
6	Reserve Bank of Australia		
7	Bank of Canada		
8	European Central Bank		
15	Bank of England		
20	Bank of Sweden		
21	Bank of Brazil		
21	Bank of Japan		
21	Federal Reserve		
22	Bank of Norway		
22	Swiss National Bank		
29	Bank of Mexico		
October			
3	Reserve Bank of Australia		
4	Reserve Bank of New Zealand		
13	Bank of Korea		
26	Bank of Brazil		
26	Bank of Canada*		
27	European Central Bank		
27	Bank of Japan		
31	Reserve Bank of Australia		
November			
2	Federal Reserve		
3	Bank of England		
3	Bank of Norway		
10	Bank of Mexico		
22	Reserve Bank of New Zealand		
23	Bank of Korea		
24	Bank of Sweden		
December			
5	Reserve Bank of Australia		
7	Bank of Brazil		
7	Bank of Canada		
14	Federal Reserve		
15	European Central Bank		
15	Bank of England		
15	Bank of Norway		
15	Bank of Mexico		
15	Swiss National Bank		
19	Bank of Japan		

NOTE: Certain banks may decide to change rates in-between the scheduled meetings. The abbreviations s.q. and b.p. correspond to status quo and basis points respectively. * Monetary Policy Report published.