Preview: Federal Reserve rate decision and SEPs due Wednesday 19th March at 18:00GMT/14:00EDT

SUMMARY: The FOMC is widely expected to leave rates on hold at its March 19th meeting. This has been the expectation since January, when Fed Chair Powell stressed a no-rush approach to future changes in policy, given the uncertainties ahead. Expectations ahead are more uncertain, however. The current dot plot signals two more rate cuts in 2025; Governor Waller has suggested that this is still his base case. Market focus has heavily been on policies from US President Trump, particularly on trade and tariffs, as well as government cost-cutting efforts. The recent turmoil in markets has been underpinned by uncertainty, with Trump chopping and changing tariff policy frequently, and when combined with cost-cutting, has been raising fears around US economic growth, with recession fears rising. The Atlanta Fed's GDPNow estimate was Q1 growth of -2.4%, however, when adjusted for gold imports, it rose from -0.4% to 0.4% after the February labour market report.

SEP: With the Summary of Economic Projections set to be updated, a lot of attention will lie on the 2025 dot plot as a signal for how many rate cuts are to be expected this year. The current dot plot implies two 25bps rate cuts in 2025, and Governor Waller has suggested that this remains his base case. The composition of the 2025 dot plot in December had ten members on the FOMC pencil in rate reductions to 3.9% by year-end (a FFR target between 3.75-4.00%), with five seeing rates below that level, and four seeing rates above that level. Money markets, at the time of writing, currently price in 65bps of easing through 2025, which fully prices two 25bp rate cuts, with a 60% probability of a third. The economic projections (PCE, GDP and unemployment) will be used to show how the FOMC expects Trump's policies to influence the economy. It may be that the unemployment rate rises, as Trump lays off thousands of government workers, while PCE expectations may rise to show the impact of tariffs. Meanwhile, increased trade tensions and ongoing uncertainty related to policies may see slower economic growth ahead.

ECONOMY: Recent data has seen consumer confidence tumble, primarily due to uncertainty ahead, which is raising concerns over consumer spending. With the February PPI and CPI report now out, PCE (due 28th March), as compiled by WSJ's Fedwatcher Timiraos, is expected to show a 0.31% rise M/M on the headline and 0.34% M/M for Core, with the Y/Y at 2.5% and 2.7%, respectively for headline and core. Fed Chair Powell may provide his own forecast at the upcoming press conference. Labour market data saw an uptick in the unemployment rate to 4.1% (vs the Fed's median projection of 4.3% for the end of this year). Nonetheless, the hard data does not fully incorporate the impact of Trump's policies, with data in the months' ahead expected to show the effect, with reciprocal tariffs set to kick in on April 2nd. Meanwhile, a new poll from NBC showed that US voters are starting 2025 sour on the state of the economy and how Trump is handling it so far. Fed Chair Powell spoke just before the blackout period, and he largely reiterated his messaging from January and February, suggesting that the recent data has not yet changed his views on the economy or policy, despite the rise in consumer inflation expectations.

RECENT COMMENTARY: The Fed continues to push the message that they are not in a rush to act on policy due to the uncertainty surrounding the impact of President Trump's policies, and have not signalled any change of approach for the March meeting. Many have said that policy is still restrictive, and is well-positioned to deal with risks. Powell continues to toe the line that the Fed can hold for longer if inflation does not return to target, but it can also cut more quickly if there is an unexpected downturn in the labour market, or indeed if inflation falls too fast. Powell acknowledged that recent data points to a possible moderation in consumer spending amid the heightened uncertainty, but it remains to be seen how these may affect future spending and investment. He stressed that the economy is fine, and it does not need the Fed to do anything. It is also worth noting that Governor Bowman said the labour market and economic activity will become a larger factor in Fed policy discussions going forward. NY Fed's Williams has been watching the consumer inflation expectations data, while Waller said he is particularly interested in market pricing of inflation expectations. The Fed has indicated that long-term inflation expectations are not becoming unanchored, but it is something that they are watching. Waller also highlighted that markets are not pricing in any serious long-term inflation; Waller is of the view that two cuts for 2025 remain a reasonable base case. Williams noted that it is difficult to know what the Fed will do with rates this year. On the impact of tariffs, Waller noted that past Trump tariffs were more modest, and saw very little passed through, but it would be very hard for businesses to eat a 25% tariff. Meanwhile, Powell said that the general thought is that a one-time jump in prices does not need a monetary policy response.

BALANCE SHEET: Any updates on the balance sheet will be key; the latest FOMC minutes noted that various participants see it as appropriate to consider pausing, or slowing balance sheet runoff until there is a resolution of debt ceiling dynamics. However, the Fed survey respondents saw the balance sheet runoff concluding by mid-2025, which is slightly later than previously expected. Meanwhile, many noted after the conclusion of balance sheet runoff, it would be appropriate to structure asset purchases to move maturity composition closer to the outstanding stock of Treasury debt. Analysts at ING point out that continued QT at the current pace would likely see bank reserves converge on USD 3tln by the middle of 2025. At this level, it represents around 10% of GDP and is seen as something of a floor that the Fed would prefer not to get too far below. When QT concludes, the Fed would be a regular buyer of Treasuries, and with USD 50-100bln rolling off on a monthly basis, the Fed would be buying that amount in order to keep their holdings unchanged.

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