

ESSENTIALS OF MONETARY POLICY

Federal Reserve (Fed)

Caught between a Rock and a Hard Place, the Fed Raises Rates 25 Points

By Francis Généreux, Principal Economist

ACCORDING TO THE FED

- ▶ The Committee decided to raise the target range for the federal funds rate by 0.25%. It is now in a range of 4.75% to 5.00%.
- ▶ The U.S. banking system is sound and resilient. Recent developments are likely to result in tighter credit conditions for households and businesses and to weigh on economic activity, hiring, and inflation. The extent of these effects is uncertain. The Committee remains highly attentive to inflation risks.
- ▶ The Committee anticipates that some additional policy firming may be appropriate in order to attain a stance of monetary policy that is sufficiently restrictive to return inflation to 2 percent over time. The Committee will closely monitor incoming information and assess the implications for monetary policy.
- ▶ Recent indicators point to modest growth in spending and production. Job gains have picked up in recent months and are running at a robust pace; the unemployment rate has remained low. Inflation remains elevated.

COMMENTS

All eyes in the economic and financial world were on this week's Federal Reserve (Fed) meeting. Two weeks ago, there was a good chance the Fed would pick up the pace of rate hikes in response to strong economic data and sticky inflation. It seemed to be telegraphing a 50-point increase after tightening by 25 points on February 1. Then Silicon Valley Bank and other financial institutions collapsed, giving markets the jitters. Suddenly the question became would the Fed shift its focus from fighting inflation to calming markets. Today it raised rates another 25 points, seemingly betting it can do both.

Why didn't the Fed hike 50 points given the hot economic data? It believes the recent banking sector turmoil will result in tighter credit conditions, making the need for rate hikes less pressing. During his press conference, Jerome Powell said a tightening in financial conditions could be seen as the equivalent of a rate hike or perhaps more than that. The Fed's dot plot calls for just one more increase, which would bring the upper end of the target range to 5.25%. But it sees one less rate cut next year, bringing rates to 4.50% by the end of 2024 instead of 4.25%. Its economic and inflation projections are largely unchanged from December.

The Fed is also betting that the special tools at its disposal will be enough to stabilize the markets. This includes the new Bank Term Funding Program to help banks meet the needs of all their depositors. Jerome Powell added that deposit flows in the banking system have stabilized over the last week.

IMPLICATIONS

Inflation is still too high and the labour market is still too tight, but financial market turmoil is complicating the Fed's job. It now has to consider how tighter credit conditions could affect the economy and ultimately inflation. Given all this—and despite resilient economic data so far this year—we expect one last rate hike in May.

2023 Schedule of Central Bank Meetings

Date	Central bank	Decision	Rate
January			
13	Bank of Korea	+25 b.p.	3.50
18	Bank of Japan	unchanged	-0.10
19	Bank of Norway	unchanged	2.75
25	Bank of Canada*	+25 b.p.	4.50
February			
1	Bank of Brazil	unchanged	13.75
1	Federal Reserve	+25 b.p.	4.75
2	European Central Bank	+50 b.p.	3.00
2	Bank of England	+50 b.p.	4.00
6	Reserve Bank of Australia	+25 b.p.	3.35
9	Bank of Sweden	+50 b.p.	3.00
9	Bank of Mexico	+50 b.p.	11.00
21	Reserve Bank of New Zealand	+50 b.p.	4.75
23	Bank of Korea	unchanged	3.50
March			
6	Reserve Bank of Australia	+25 b.p.	3.60
8	Bank of Canada	unchanged	4.50
10	Bank of Japan	unchanged	-0.10
16	European Central Bank	+50 b.p.	3.50
22	Bank of Brazil	unchanged	13.75
22	Federal Reserve	+25 b.p.	5.00
23	Bank of England		
23	Bank of Norway		
23	Swiss National Bank		
30	Bank of Mexico		
April			
4	Reserve Bank of Australia		
4	Reserve Bank of New Zealand		
12	Bank of Canada*		
13	Bank of Korea		
26	Bank of Sweden		
28	Bank of Japan		
May			
2	Reserve Bank of Australia		
3	Bank of Brazil		
3	Federal Reserve		
4	European Central Bank		
4	Bank of Norway		
11	Bank of England		
18	Bank of Mexico		
23	Reserve Bank of New Zealand		
25	Bank of Korea		
June			
6	Reserve Bank of Australia		
7	Bank of Canada		
14	Federal Reserve		
15	European Central Bank		
16	Bank of Japan		
21	Bank of Brazil		
22	Bank of England		
22	Bank of Norway		
22	Bank of Mexico		
22	Swiss National Bank		
29	Bank of Sweden		

Date	Central bank	Decision	Rate
July			
4	Reserve Bank of Australia		
11	Reserve Bank of New Zealand		
12	Bank of Canada*		
13	Bank of Korea		
26	Federal Reserve		
27	European Central Bank		
28	Bank of Japan		
August			
1	Reserve Bank of Australia		
2	Bank of Brazil		
3	Bank of England		
10	Bank of Mexico		
15	Reserve Bank of New Zealand		
17	Bank of Norway		
24	Bank of Korea		
September			
5	Reserve Bank of Australia		
6	Bank of Canada		
14	European Central Bank		
20	Bank of Brazil		
20	Federal Reserve		
21	Bank of England		
21	Bank of Norway		
21	Swiss National Bank		
22	Bank of Japan		
28	Bank of Mexico		
**	Bank of Sweden		
October			
2	Reserve Bank of Australia		
3	Reserve Bank of New Zealand		
19	Bank of Korea		
25	Bank of Canada*		
26	European Central Bank		
31	Bank of Japan		
November			
1	Bank of Brazil		
1	Federal Reserve		
2	Bank of England		
2	Bank of Norway		
6	Reserve Bank of Australia		
9	Bank of Mexico		
28	Reserve Bank of New Zealand		
30	Bank of Korea		
**	Bank of Sweden		
December			
4	Reserve Bank of Australia		
6	Bank of Canada		
13	Bank of Brazil		
13	Federal Reserve		
14	European Central Bank		
14	Bank of England		
14	Bank of Norway		
14	Bank of Mexico		
14	Swiss National Bank		
19	Bank of Japan		

NOTE: Central banks may decide to change rates between the scheduled meetings. The abbreviation b.p. stands for basis points. * Monetary Policy Report published; ** To be determined.