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Research

Economics
Fed Notes

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March FOMC recap: No (core goods) inflation progress, no rate cut

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- The Fed held rates steady and the key elements of the meeting were in line with expectations. The statement noted the uncertainty caused by recent events in the Middle East, the median dot continued to show one rate cut for this year, and Powell's messaging skewed hawkish on inflation, but did not actively push for a balanced description of the policy outlook – rate cuts may be less likely but are still more likely than hikes.
- Aside from the growth forecasts, the SEP revisions were in line with expectations. Real GDP growth was revised 10-30bps higher across the forecast horizon, including the longer-run estimate. Powell noted that this likely reflected ongoing strength in productivity growth – a key reason why the unemployment rate forecasts were mostly unchanged. Inflation was revised slightly higher over the next two years. Though policy rate expectations compressed somewhat, the median rate estimates were unchanged from the December meeting.
- Powell unexpectedly made news on his future, committing to remain on the Board until the DoJ investigation is "well and truly over." While he said he would stay on as Chair pro tempore until his successor is confirmed, Powell has not decided if he would otherwise remain on the Board after the DoJ investigation is resolved.
- Today's messaging was consistent with our baseline expectations that Powell delivered his final rate cut last December and that the Fed is likely to only deliver one reduction this year in September. Indeed, the SEP is very close to our own expectations. That said, as long as the labor market remains broadly stable, inflation concerns could push the Fed to remain on hold for longer.

Statement

As expected, the FOMC maintained the fed funds rate at 3-1/2 to 3-3/4 percent, though there were fewer dissents to this decision than we thought there could have been. Notably, only Governor Miran dissented in favor of a quarter point rate cut.

In terms of changes to the statement, there were only two, both of which were in line with our expectations. First, the Committee continued to note that job gains have "remained low", but they slightly upgraded the language around the unemployment rate from "show[ing] some signs of stabilization" to "has been little changed in recent months." Second, as they did at the onset of the Ukraine/Russia crisis, the second paragraph noted that the "implications of developments in the Middle East for the U.S. economy are uncertain."

Summary of Economic Projections (SEP)

Revisions to the SEP were also largely in line with our prior expectations. Most importantly, the median forecasts for the policy rate out to 2028 were unchanged from December (3.4% for 2026, 3.1% for 2027 and 2028), though the median long-run dot ticked up by a tenth to 3.1%. Revisions to the economic forecasts seemed to be mostly a function of better productivity growth momentum, potentially due to productivity gains from AI, plus the supply shock from higher energy prices. Median growth forecasts were revised up across the forecast range: 2026 up a tenth to 2.4%, 2027 up three-tenths to 2.3%, 2028 up two tenths to 2.1%, and longer-run growth up two-tenths to 2.0%. However, the unemployment rate forecasts were mostly unchanged—hinting at productivity driving the growth upgrades; 2026 UR remained at 4.4%, 2027's increased by a tenth to 4.3%, and 2028's remained at 4.2% as did the longer-run estimate.

At the same time, the median forecast for inflation shifted higher, likely reflecting the recent increases to energy prices as well as the latest data on trends in core. Headline and core increased by three- and two-tenths respectively, both to 2.7%. Similarly, 2027's forecast for both inflation measures increased by a tenth to 2.2%, while 2028's forecasts remained at 2.0%.

In the dot plot, there were some hawkish innovations under the surface. While three dots for 2027 came down from 3.875% to 3.625% - reflecting a mark-to-market after the "silent dissents" to the December rate cut – one official penciled in a rate hike in 2027. Perhaps more notably, several of the participants on the dovish side trimmed their expectations for rate cuts this year, as had been signaled before the meeting by Governor Miran.

Press conference

Chair Powell's press conference focused heavily on inflation developments and outlook, more than potential concerns around the labor market. This skew gave a hawkish tone to the discussion. Case in point, while inflation was mentioned 67 times, the labor market/employment/unemployment was only referenced 40 times. Most surprisingly, uncertain/uncertainty were only used 7 times.

On inflation, Powell continued to focus on tariff-driven inflation in the core goods category. He noted that tariffs have likely added one-half to three-quarters of a percentage point to inflation and maintained the view that these effects are likely to begin to wane around the middle of the year. Powell argued that seeing core goods disinflation is "really important" for determining the potential for rate cuts in the back half of the year.

Notably, Powell removed a line on disinflation for core services in his prepared remarks, potentially reflecting the strengthening in super core inflation that has occurred in recent months. When pressed on how the Fed is thinking about this category, Powell attributed the stickiness to a "bunch of idiosyncratic things", and that they continue to expect progress to eventually return to this category.

While the ongoing oil price shock will no doubt lift headline inflation, Powell expressed uncertainty about what the pass-through is likely to be to core inflation. Nonetheless, he sounded more concerned about the continued overshoot of the inflation objective, now five years after the Covid-driven inflation originated. Powell noted that they are "well aware" of this history, but that they do not want to "overreact" to current inflationary pressures simply based on that experience. Powell emphasized that they need to remain vigilant on inflation and ensure that inflation expectations remain well anchored at 2% in the presence of another oil price shock. This discussion leaned hawkish, particularly compared to his relatively sanguine views on inflation in recent press conferences.

In contrast to recent press conferences, there was more limited focus on the labor market. Powell pointed to stability in the unemployment rate as being more important than weakness in payroll gains, which continue to be under downward pressure from constrained labor supply due to immigration policies. Consistent with our view, Powell argued for averaging through the past two volatile jobs reports, noting that the February payrolls print was likely distorted lower by ~80k due to a strike and weather effects. Moreover, Powell noted that after accounting for potential future downward revisions, private sector payroll gains have likely been near zero, which he suggested could well be near the breakeven rate.

In terms of near-term policy, the signal was that the Fed is "well positioned" to respond to developments and that the Fed can wait for some clarity on the outlook to emerge over the coming months. Powell downplayed the signal from the SEP even more than usual, given heightened uncertainty from events in Iran. He even stated that officials noted that, if there was ever a time to skip the SEP, this was one of them.

When asked about the potential for rate hikes, Powell noted that a "vast majority" of officials do not anticipate rate increases, consistent with only one official anticipating a rate hike next year. He also did not suggest that more officials argued for a balanced description of the policy outlook relative to January, where the minutes noted "several officials" could support that description. In this way, Powell did not actively push for a balanced description of the policy outlook. That said, Powell pushed back on the notion that downside risks to the labor market exceed upside risks to inflation. Together, we interpreted these comments as suggesting the case for rate cuts has weakened but remains stronger than the case for rate hikes.

What is the story for rate cuts then? Powell noted that each official may have his/her own story, but that overall that case relies on disinflation progress returning – most likely due to core goods disinflation later this year -- and allowing policy to move closer to neutral policy over time. Powell described the current policy-setting as within a range: in the upper end of neutral or moderately/modestly restrictive. He noted that this stance is appropriate at this point, to ensure that inflation does move back to target over time.

One area where Powell made unexpected news was about his future. Specifically, Powell committed to remain on the Board until the DoJ investigation is "well and truly over." He also stated he would stay on as Chair pro tempore until his successor is confirmed, as has been done in the past. However, Powell did not commit to whether he would remain on the Board after the DoJ investigation is resolved.

Finally, Powell noted that AI could lift the neutral rate, given its potential to boost investment demand and lift productivity. That stronger productivity growth story was initially due to the response to a historically tight labor market but could increasingly be due to AI as we look ahead. This was likely one factor supporting the upward adjustment in the longer-run growth projection.

Overall, today's messaging was consistent with our baseline expectations that Powell delivered his final rate cut last December and that the Fed is likely to only deliver one reduction this year in September. Indeed, the SEP is very close to our own expectations. That said, as long as the labor market remains broadly stable, inflation concerns could push the Fed to remain on hold for longer.

Appendix 1

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