Metrobank
Research and Market Strategy Department

POLICY RATE VIEWS

THE CYCLE CONTINUES: FED TO SUPPORT THE LABOR MARKET

Fed cuts by 25 bps

The US Federal Reserve (Fed) reduced the Federal Funds Target Rate (FFR) by 25 basis points (bps) to 4.50% - 4.75% during the Federal Open Market Committee (FOMC) meeting on November 6-7, US time, as widely expected by the market. This was the second adjustment for the FOMC after holding policy rates steady for eight consecutive meetings.

US Economy on Track

In its November statement, the FOMC continued to acknowledge that labor market conditions have generally eased and that inflation, although somewhat still elevated, continues to make further progress toward the 2% target.

In his speech following the latest committee meeting, FOMC Chair Jerome Powell acknowledged that payroll job gains has been weak, averaging only 104,000 in the past three months, weighed down by the effects of labor strikes and hurricanes. He also maintained that inflation has "moved much closer" to the 2% longer-run goal, and consumer-price rise expectations remain well-anchored.

In the same speech, Powell also highlighted a strong US economy that has continued to expand at a solid pace. He acknowledged that the growth of consumer spending has remained resilient, and that investment spending has strengthened, although activity in the housing sector has been weak.

Fed Funds Target Rate as of November 8, 2024

4.50% to 4.75%

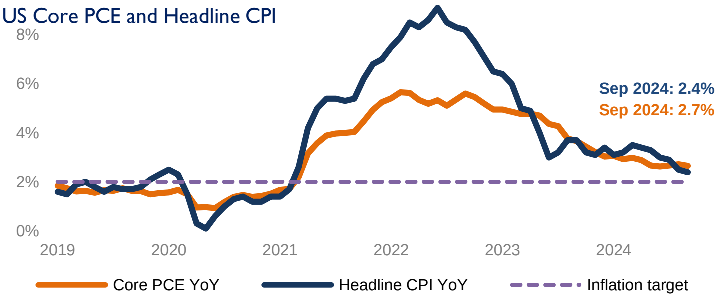
US Economic Data

Fed's preferred inflation measure, the US Core Personal Consumption Expenditure (Core PCE) Price Index, has been on an upward trend since July, accelerating further at 2.7% year-on-year (YoY) in September and bringing year-to-date (YTD) inflation to 2.8%. Services inflation remains the biggest contributor, contributing 2.6 percentage points (ppts) out of the total 2.7%. On a month-on-month (MoM) basis, core PCE also increased to 0.3% in September from the upwardly revised 0.2% in the preceding month.

Meanwhile, headline Consumer Price Index (CPI) decelerated further to 2.4% YoY in September, bringing down the YTD inflation rate to 3.0%. Although decelerating, the sticky shelter prices remain the major driver of CPI inflation. On a month-on-month basis, headline CPI accelerated by 0.2% for the third consecutive month in September.

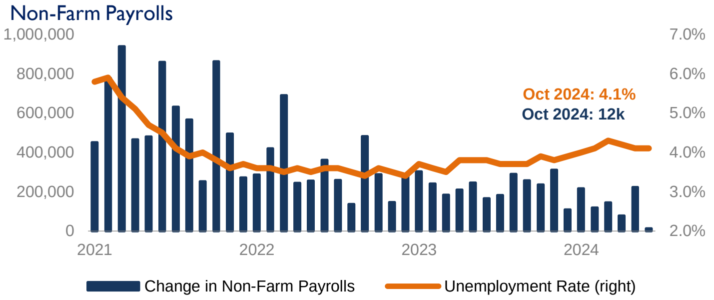
The job market nearly stalled in October amid hurricane disruptions and Boeing labor union strikes, with Non-Farm Payrolls increasing only by 12,000, significantly lower than the consensus estimate of 100,000 for the month. New Non-Farm Payrolls in August have been revised downward to 78,000 from the earlier reported, supporting view of a continuously cooling labor market. Unemployment rate in October remained at 4.1%, the same as the preceding month.

US Inflation
US Core PCE and Headline CPI



Source: Bloomberg

US Labor Market
Non-Farm Payrolls



Source: Bloomberg

METRO RESEARCH'S TAKE

The recent policy movement by the Fed was aligned with Metrobank Research's expectation. We maintain our forecast that the Fed will continue with its easing cycle and deliver a total of 100 bps of cuts for FY 2024, bringing the FFR to 4.25%-4.50% by year-end. We continue to expect the Fed to deliver cumulative cuts worth 100 bps in 2025 and 50 bps in 2026. This should bring the target FFR to its terminal rate of 3.00% by end-2026.

On the domestic front, Metrobank Research maintains its view that the BSP will reduce its policy rate by another 25 bps in its last Monetary Board meeting in December to further support growth. This would bring the BSP's target reverse repurchase (RRP) rate down to 5.75% by year-end, settling at a 125-bp interest rate differential between the BSP and the Fed. We also expect 100 bps worth of cuts in 2025 and another 50 bps worth of cuts in 2026, which would bring down RRP to 4.25% by end-2026.

The strength of the dollar pre-US election was ascertained by expectations of Former US President Donald Trump's return to the White House in 2025. The dollar index at a 4-month high a day after the US national elections. However, we saw a slight reversal in the strength of the greenback after the Fed's recent 25-bps cut.

With the control of the lower house in the US Congress still in question, Metrobank Research sees two potential scenarios on the movement of USD/PHP, also taking into account proposed policies in the new US administration and the expected support to the peso from incoming Business Process Outsourcing companies' bonuses and from overseas Filipino workers' remittances in Q4.

Should the Republicans take majority of the seats in the lower house, thus allowing full control of the US national government, we expect peso depreciation toward the end-2024 with the USD/PHP spot possibly settling at 58.8. Otherwise, we expect the reversal to continue and see spot ending relatively lower at 56.9 by year-end.