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Jackson Hole Economic Symposium: All eyes on where interest rates are headed

At the annual meeting of global central bankers and policymakers that concluded on Friday, 25 August 2023, in Jackson Hole, Wyoming, United States Federal Reserve (Fed) Chairman Jerome Powell delivered a closely watched speech on the Fed's interest rate outlook. Powell highlighted that the central bank's policy decision will be guided by economic data, leaving policy guidance open-ended, but emphasised that the fight against inflation is not over. Market expectations on monetary policy remained unchanged after his speech, and investors currently still have the opportunity to enjoy higher yields.

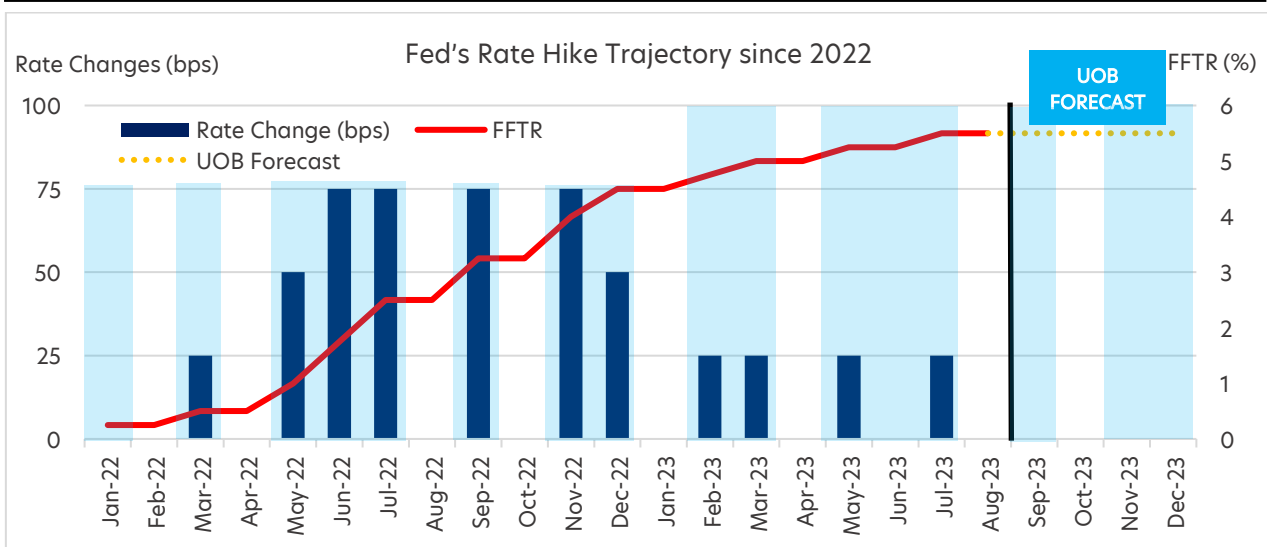
Five key takeaways from Fed Chairman Jerome Powell's speech

1. Inflation could reaccelerate, and the Fed is prepared to respond if required
 - Despite improvements in the inflation situation, the central bank remains prepared to raise interest rates further, as the resilience of the US economy could result in inflation rising again.
2. Fed may keep interest rates unchanged in September
 - The Federal Funds Target Rate (FFTR), which is the target interest rate range set by the Fed, is likely to remain unchanged at the next Federal Open Market Committee (FOMC) meeting in September. This projection is aligned with Powell's remarks that monetary policy is now restrictive, and that the Fed will "proceed carefully" as they assess incoming data as well as the evolving economic outlook and risks.
3. A new phase in policymaking has arrived
 - Policymaking has shifted to a new phase where policymakers are now sensitive to the risk of hiking rates too much. This is seen by how the pace of rate hikes has slowed from 75 basis points (bps) to 25 bps over the past eight months, with a potential pause in rate hikes ahead.
 - Powell hinted that policy decisions are now more deliberate and repeatedly emphasised risk management in future policy decisions, since interest rates are high enough to be restrictive and weigh on economic growth and inflation.
4. Labour market and economic growth will be closely monitored
 - In line with the Fed's focus on economic data guiding their next steps, upcoming job market and economic growth reports will be closely monitored. Powell indicated that strong growth and a strengthening of the labour market could lead to higher inflation and therefore justify higher rates.
5. 2% inflation remains the target, but it is difficult to estimate the neutral policy rate
 - Despite suggestions that the Fed should raise the inflation target above 2% due to fundamental changes in price pressures post-pandemic, Powell insisted that 2% "is and will remain our inflation target". He also stressed the difficulty in identifying the neutral policy rate which is defined as the rate at which monetary policy is neither stimulating nor restricting economic growth.

Our view: Policy rates are at or near the peak. However, no rate cuts are expected this year.

- We reaffirm our view that the Fed will be on pause for the upcoming FOMC meeting in September and for the rest of the year, with the Fed Funds Target Rate (FFTR) kept at 5.25%-5.50%.
- Since the Fed's policy rate is already in restrictive territory, it is unclear if and when the impact of prior aggressive rate hikes will result in slower economic growth.
- Nonetheless, there remains risk that the Fed could hike a final 25 bps if inflation shows signs of heating up again.
- We continue to expect no rate cuts in 2023, with potential rate cuts only likely from 1Q 2024 onwards.

UOB's Projected US Federal Funds Target Rate Trajectory (as of 28 Aug 2023)



Source: UOB PFS Investment Strategists, UOB Global Economics & Markets Research.

What you can do

- The spike in bond yields after the Jackson Hole meeting may be temporary. Though inflation may reaccelerate due to higher oil and food prices, the Fed may choose to look past these temporary factors and focus on the broader trend of slowing price pressures. Investors have the opportunity to lock in higher yields with bond funds and investment grade (IG) bonds, as the global monetary tightening cycle is nearing the end.
- As the global economy slows further, high-quality bonds can be expected to help investors withstand macroeconomic uncertainties better than riskier investments.
- In the current market environment, build resilient portfolios to work towards your long-term financial goals and avoid concentrating your investments in any one sector or market. Global multi-asset strategies can also help lower overall portfolio volatility.
- If you have appropriate risk appetite for tactical market opportunities, consider our Top Ideas of Asia ex-Japan/China/ASEAN to tap on China's re-opening, as well as Global Healthcare to ride on the long-term trend of an ageing global population.
- Speak to a UOB Advisor on how to position your portfolio according to your risk appetite and goals.



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