Economic Update

May 23, 2024

FOMC Minutes: Less Progress on Inflation, More Uncertainty About the Path of Monetary Policy

- **The minutes from the latest FOMC meeting noted that participants still expected inflation to ease, but that progress in reducing inflation had slowed in early 2024.**
- **Participants expected a slowing in economic growth this year and a better balance between supply and demand in the labor market.**
- **The minutes noted greater uncertainty about the long-run neutral fed funds rate.**
- **PNC expects two fed funds rate cuts in the second half of 2024 and additional rate cuts next year.**

According to the minutes from the Federal Open Market Committee meeting on April 30 and May 1, committee members noted that progress in moving inflation toward the 2% target had slowed in the first part of 2024. The minutes say that while participants agreed that inflation would slow to 2% over the medium term, “recent data had not increased their confidence in progress toward 2% and, accordingly, had suggested that the disinflation process would likely take longer than previously thought.” However, participants did expect that inflation would slow in the near term, from both slower rent growth and an easing in wage pressures. There was also some optimism about stronger productivity growth that could help slow inflation. And some participants reported that business contacts were reporting greater consumer pushback against price increases.

Participants generally reported that the labor market was moving back into better balance between supply and demand, with slower wage growth. In part this better balance came from greater supply thanks to higher labor force participation and more immigration.

Participants expected GDP growth to slow in 2024 from 2023. In particular consumer spending growth was expected to ease with slower job and wage growth. There were also indications that lower- and middle-income households are facing greater financial pressures that would weigh on spending. However, upper-income households continued to benefit from increased wealth from rising equity prices and home values.

There were concerns that problems in commercial real estate markets could be a drag on the economy. There were also concerns about potential stresses in less regulated parts of the financial system, exacerbated by high interest rates.

Participants agreed that the risks to the committee’s objectives for a strong labor market and price stability had moved into better balance over the past year. But there was increased uncertainty about the impact of monetary policy. The minutes say that “although monetary policy was seen as restrictive, many participants commented on their uncertainty about the degree of restrictiveness.” This uncertainty came from the possibility that monetary policy now is less effective that it was in the past, that the neutral long-run fed funds rate may be higher than previously thought, or that long-run economic growth may be lower than previously thought.

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The minutes specifically say that “various participants mentioned a willingness to tighten policy further should risks to inflation materialize in a way that such an action become appropriate.” That being said, the likelihood of near-term fed funds rate increases remains low given the slowing in inflation expected later this year.

There was some discussion about the announcement about the slowing in the pace of reduction in the Federal Reserve’s balance sheet. The FOMC announced on May 1 that it will cap the reduction in long-term Treasury securities at $25 billion per month starting in June, down from $60 billion per month currently. The Fed will continue to reduce its holdings of mortgage-backed securities by up to $35 billion per month. Some participants thought that the $25 billion cap should be larger.

The minutes from the latest FOMC meeting are consistent with PNC’s forecast for two cuts in the fed funds rate in the second half of 2024, each of 25 basis points. After less progress in slowing inflation in the first few months of 2024, inflation should cool further through the rest of this year due to slowing rental inflation and easing wage pressures. This would make the FOMC more comfortable that inflation is moving to 2% and allow for a modest easing in monetary policy. Monetary policy would still be restrictive, weighing on economic growth, just somewhat less so than before the cuts to the fed funds rate. PNC then expects additional fed funds rate cuts in 2025 as inflation slows further.

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