Economic Update

March 19, 2025

FOMC Keeps Fed Funds Rate Unchanged, Slows Pace of Balance Sheet Reduction; Fed Funds Rate Path Unchanged from December

- **The FOMC held the fed funds rate unchanged in a range between 4.25% and 4.50%.**
- **The Fed will allow up to $5 billion of long-term Treasurys to roll over the balance sheet per month starting in April, down from $25 billion currently. MBS runoff will remain at $35 billion.**
- **Projections for the fed funds rate in the dot plot were unchanged from December, with two 25 basis point cuts expected in 2025.**
- **Expectations for near-term growth in the dot plot were slightly lower, with expectations for inflation slightly higher.**
- **In his press conference Chair Powell specifically noted heightened uncertainty.**
- **PNC's baseline forecast has two cuts of 25 basis points each in the fed funds rate this year.**

As expected, the Federal Open Market Committee kept the fed funds rate unchanged this afternoon, in a range between 4.25% and 4.50%. The FOMC cut the fed funds rate sharply to near zero at the start of the pandemic, and then rapidly increased the fed funds rate in 2022 and 2023 to above 5%. The FOMC cut the fed funds rate by a cumulative 100 basis points from September to December last year, to its current range. But the FOMC has now held the fed funds rate steady at its last two meetings.

The change in monetary policy came in the Fed's balance sheet. The FOMC announced that starting in April, the central bank will reduce its holdings of long-term Treasurys by $5 billion a month, down from $25 billion a month. The Fed will continue to let up to $35 billion a month in maturing mortgage-backed securities to roll off the balance sheet. This will further shift the Fed's balance sheet toward holding mostly Treasurys. In his post-meeting press conference, Fed Chair Jerome Powell said the decision to slow the pace of balance sheet reduction was based in part on "some signs of tightness in money markets."

The Fed rapidly increased the size of its balance sheet in 2020 and 2021 by creating money electronically and using the proceeds to purchase long-term Treasurys and MBS; this pushed down long-term borrowing costs, supporting the economic recovery from the pandemic. But as the economy recovered and inflation picked up the Fed started to reduce the size of its balance sheet in 2022. Now the Fed appears to be winding down that process. The Fed's balance sheet was below $4 billion before the pandemic, peaked at close to $9 billion in early 2022, and is now around $6.5 billion.

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This FOMC meeting also included the release of the Summary of Economic Projections, or "dot plot," which is updated every three months. The outlook for the fed funds rate is unchanged compared to the previous dot plot, in mid-December. The median FOMC participant anticipates two 25 basis point cuts in the federal funds rate this year, taking it to around 3.9% by the end of 2025. The median participant then has the fed funds rate at 3.4% at the end of 2026 and 3.1% at the end of 2027; 3.1% is also the median value of the long-run fed funds rate.

Expectations for economic growth in 2025 have been marked down. The median participant has real GDP growth of 1.7% this year in today's dot plot, compared to 2.1% in the December dot plot. Growth was also marked down somewhat in 2026 and 2027.

There was little change to the projections for the unemployment rate. The median participant has the rate at 4.4% at the end of this year, compared to 4.3% in the December dot plot. The median unemployment rate is 4.3% at the ends of 2026 and 2027 in today's release, unchanged from December.

Near-term inflation projections have been marked up somewhat. The median participant has core PCE inflation at 2.8% at the end of 2025 today, compared to 2.5% in December. Presumably at least some of this is due to expected higher tariffs. Median projected core inflation in 2026 is projected to slow to 2.2%, unchanged from December.

The statement underwent a few changes compared to the previous one, from January 29. In new language, today's statement said that "uncertainty around the economic outlook has increased," presumably in response to tariffs and federal spending and job cuts from the Trump administration. Today's statement removed language from late January that said that "risks to achieving [the] employment and inflation goals are roughly in balance."

The statement was not approved unanimously. Fed Governor Waller supported no change in the fed funds rate, but wanted to continue to reduce Fed holdings of long-term Treasurys by $25 billion per month.

In his press conference, Powell noted higher uncertainty about the economic outlook, specifically noting tariffs, immigration, fiscal policy, and regulation. But he also said that the FOMC does "not need to be in a hurry" to change the federal funds rate.

Today's statement and dot plot held few surprises. Expectations were very high for no change in the fed funds rate, and the central bank was expected to slow the pace of the reduction in balance sheet, if not today then at the next meeting, in early May. There was more uncertainty about the dot plot. But the FOMC outlook for the fed funds rate was unchanged from December. There was more movement in the economic projections, with slower growth and higher inflation expected this year compared to December.

PNC's baseline March forecast has two 25 basis point cuts in the fed funds rate in 2025, in May and July. But depending on inflation readings over the next few months, those rate cuts could be pushed out later into 2025. These cuts would take the fed funds rate to a range of 3.75% to 4.00% by the end of 2025.

Stocks rose slightly after the release of the statement, while the yield on the 10-year Treasury note fell by a couple of basis points. There was little change in the 3-month T-bill yield. The dollar weakened slightly against a basket of currencies. The price of a barrel of West Texas Intermediate crude oil was little changed at somewhat above $67.

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