RBC Economics & Thought Leadership

Economic Update

June 14, 2023

Fed skips June hike but suggests more tightening to come

- As expected, the Fed took a pass on raising rates for the first time in 15 months
- Decision looks more like a skip than a pause with July hike expected
- In a hawkish surprise, the dot plot shows most committee members (12 of 18) expect at least 50 bps of further tightening this year

The Fed opened the door to a pause at its May meeting and followed through today by holding fed funds steady at 5.00-5.25%. But with recent data remaining on the firm side and banking concerns receding, the vast majority of committee members think further tightening is needed. So as a number of Fed officials suggested pre-blackout period, this is more of a “skip” than a pause. And it’s a hawkish skip at that. The updated dot plot shows a 2023 median of 5.50-5.75%, up 50 bps from March’s SEP and 25 bps above expectations.

There were few changes to the policy statement with language introduced in May continuing to give the Fed plenty of optionality. Today’s steady decision was explained as allowing the FOMC to “assess additional information and its implications for monetary policy.” Chair Powell elaborated that the committee saw a further slowing in the pace of rate hikes as a natural progression in the Fed’s tightening cycle as it gets closer to terminal. That would seem to suggest an every-other-meeting pace going forward though Powell said that decision was not made today.

Underpinning a higher expected terminal rate, the committee’s median 2023 GDP growth forecast (Q4/Q4) rose to 1.0% from 0.4% previously and its Q4/23 unemployment rate projection was lowered by 0.4 ppts to 4.1%. Core PCE inflation is seen just shy of 4% by year-end, down only slightly from the recent 3-month run rate (4.3% annualized). Our forecast assumes that with the tightening delivered thus far, the economy will slow to a greater extent and unemployment will rise further than the Fed is projecting in the second half of the year. But we don’t think there will be sufficient evidence of that over the next six weeks and look for a 25 bp hike in July. Risks around our terminal rate forecast (5.25-5.50%) are skewed to the upside though at an every-other-meeting pace November is a long way away.

Josh Nye | Senior Economist, RBC Economics | Royal Bank of Canada | T. (416) 974-3979

For more economic research, visit our website at *https://thoughtleadership.rbc.com/economics/*