Moving at a slower pace

UBS Asset Management l The Fed remains committed to bringing inflation down

The Fed raised rates by a slower pace of 25 basis points.

The Federal Open Market Committee (FOMC) of the US Federal Reserve hiked rates as expected at their 1st February meeting by 25 bps, moving the fed funds target range to 450 bps – 475 bps from 425 bps – 450 bps. The vote for the rate hike was once again unanimous at 12-0.

The meeting statement contained some small changes relative to the last meeting in December. The FOMC acknowledged that inflation "has eased somewhat but remains elevated." Even as there has been improvement in CPI and other inflationary measures, the FOMC still considers current levels as too high. This view likely caused them to maintain the language that the "ongoing increases" in the federal funds target range will be needed to bring inflation back to their 2% goal. The plural nature of "increases" signals that perhaps at least two more rate hikes are anticipated by the Fed unless economic conditions deviate from their forecasts. The slight change to the use of "extent" versus "pace" of increases later in the statement was probably meant to convey that 25 bps is likely going to be the pace of future rate increases versus the more elevated cadence of 50 or 75 bps seen last year.

Fed Chair Powell noted during his press conference that "a couple more hikes" will get the Fed to the appropriately restrictive level of policy that they are seeking. He also mentioned "disinflation" for the first time, saying that the economy is in the "early states of disinflation" but that the Fed needs to see it spread across the economy, in particular the core services ex-housing sector. More broadly, he acknowledged that the market's view on inflation is different than the Fed's, but also mentioned that if inflation cools more quickly than the Fed's forecast then that "will play into our policy setting." On financial conditions, Fed Chair Powell downplayed the recent easing and instead pointing to the cumulative tightening that has occurred over the past year.

Overall, the markets interpreted Chair Powell's press conference as dovish. The market latched onto the comments about financial market conditions and the seemingly lack of firm commitment to the December dot plot forecast. The S&P 500 finished the day +1.05% and, which the 2yr Treasury fell by 9.5 bps. Fed funds futures are now showing 20 bps of hikes for the March meeting, with a year-end rate of 4.40%.

We continue to position our UBS money market funds to take advantage of this rate hike along with future ones.

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UBS Asset Management (Americas) Inc., 787 Seventh Avenue , New York, NY 10019
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