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Federal Reserve Monitor | North America

December FOMC Quick Reaction

The Fed cut 25bp as expected. The Statement came slightly more dovish than expected. Even though it included the "extent and timing" language, it no longer describes the unemployment rate as low. The SEP changed little, but with higher GDP growth in 2026 and 2027 and lower inflation.

Key Takeaways

- The Fed lowered the target fed funds range by 25bp to 3.5 - 3.75% as expected.
- The Committee remains divided. Presidents Goolsbee and Schmid dissented in favor of a hold, Gov Miran supported a 50bp cut.
- The dots indicate that 6 members would have preferred a hold this meeting.
- The SEP revised 2026 growth up and inflation down, perhaps reflecting higher expected productivity growth.

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Quick Reaction

The Fed lowered the target fed funds range by 25bp to 3.5-3.75% as expected. The statement was slightly more dovish than we expected. The Committee removed the wording that the unemployment rate "remained low". As we expected, they added the language around the "extent and timing" of further adjustments. This suggests a move from risk management cuts to a more data dependent outlook. There were three dissents; Reserve bank Presidents Goolsbee and Schmid dissented in favor of a hold while Governor Miran dissented in favor of a 50bp cut. There were more silent dissents: 6 dots showed appropriate monetary policy for 2025 would not have included today's cut.

The Committee has decided that reserve balances have declined to ample levels and will initiate purchases of shorter-term Treasury securities as needed on an ongoing basis.

The SEP included minimal changes to projections for this year, but a large upward revision to growth in 2026. Inflation projections were revised down slightly for this year and next. The combination of faster growth, slower inflation, and no difference in the unemployment rate suggests some are building in faster productivity growth. The median dot still shows 1 cut for next year and 1 cut for 2027. Next year's dots are very split, ranging from three dots at 3.75-4.0% to a dot at 2.0-2.25%, with varied views inbetween.

Changes to statement from October:

- Removed "the unemployment rate has edged up but remained low" and instead just said "the unemployment rate has edged up through September."
- Added "In considering *the extent and timing* of additional adjustments to the target range for the federal funds rate ..."
- "The Committee judges that reserve balances have declined to ample levels and will initiate purchases of shorter-term Treasury securities as needed to maintain an ample supply of reserves on an ongoing basis."

Consistent language with October:

- "... economic activity has been expanding at a moderate pace."
- Inflation remains "somewhat elevated."

Exhibit 1: December statement changes from October

Available indicators suggest that economic activity has been expanding at a moderate pace. Job gains have slowed this year, and the unemployment rate has edged up ~~but remained low~~ through ~~August~~; ~~more~~ September. ~~More~~ recent indicators are consistent with these developments. Inflation has moved up since earlier in the year and remains somewhat elevated.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. Uncertainty about the economic outlook remains elevated. The Committee is attentive to the risks to both sides of its dual mandate and judges that downside risks to employment rose in recent months.

In support of its goals and in light of the shift in the balance of risks, the Committee decided to lower the target range for the federal funds rate by 1/4 percentage point to 3-1/2 ~~to 3-3/4~~ to 4 percent. In considering the extent and timing of additional adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. ~~The Committee decided to conclude the reduction of its aggregate securities holdings on December 1.~~ The Committee is strongly committed to supporting maximum employment and returning inflation to its 2 percent objective.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

The Committee judges that reserve balances have declined to ample levels and will initiate purchases of shorter-term Treasury securities as needed to maintain an ample supply of reserves on an ongoing basis.

Voting for the monetary policy action were Jerome H. Powell, Chair; John C. Williams, Vice Chair; Michael S. Barr; Michelle W. Bowman; Susan M. Collins; Lisa D. Cook; ~~Austan D. Goolsbee~~; Philip N. Jefferson; Alberto G. Musalem; and Christopher J. Waller. Voting against this action were Stephen I. Miran, who preferred to lower the target range for the federal funds rate by 1/2 percentage point at this meeting; ~~and Austan D. Goolsbee~~ and Jeffrey R. Schmid, who preferred no change to the target range for the federal funds rate at this meeting.

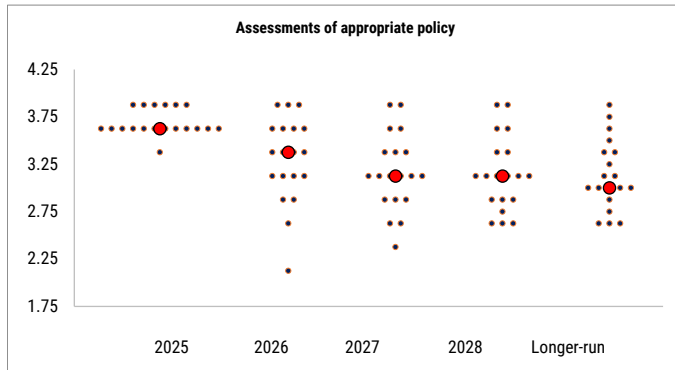
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 2: Summary of Economic Projections

| Changes to the Summary of Economic Projections | | | | | |
|--|------|------|------|------|------------|
| | 2025 | 2026 | 2027 | 2028 | Longer Run |
| Real GDP (% 4Q/4Q) | | | | | |
| December | 1.7 | 2.3 | 2.0 | 1.9 | 1.8 |
| September | 1.6 | 1.8 | 1.9 | 1.8 | 1.8 |
| <i>Difference</i> | 0.1 | 0.5 | 0.1 | 0.1 | 0.0 |
| Unemployment Rate (4Q Avg) | | | | | |
| December | 4.5 | 4.4 | 4.2 | 4.2 | 4.2 |
| September | 4.5 | 4.4 | 4.3 | 4.2 | 4.2 |
| <i>Difference</i> | 0.0 | 0.0 | -0.1 | 0.0 | 0.0 |
| Headline PCE Inflation (% 4Q/4Q) | | | | | |
| December | 2.9 | 2.4 | 2.1 | 2.0 | 2.0 |
| September | 3.0 | 2.6 | 2.1 | 2.0 | 2.0 |
| <i>Difference</i> | -0.1 | -0.2 | 0.0 | 0.0 | 0.0 |
| Core PCE Inflation (% 4Q/4Q) | | | | | |
| December | 3.0 | 2.5 | 2.1 | 2.0 | |
| September | 3.1 | 2.6 | 2.1 | 2.0 | |
| <i>Difference</i> | -0.1 | -0.1 | 0.0 | 0.0 | |
| Fed Funds Target | | | | | |
| December | 3.6 | 3.4 | 3.1 | 3.1 | 3.0 |
| September | 3.6 | 3.4 | 3.1 | 3.1 | 3.0 |
| <i>Difference</i> | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

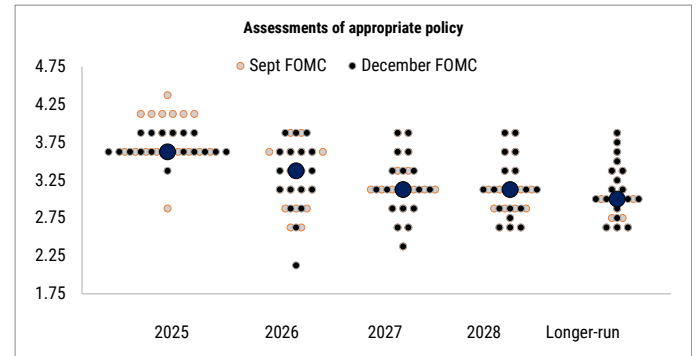
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 3: December dot plot



Source: Federal Reserve Board, Morgan Stanley Research

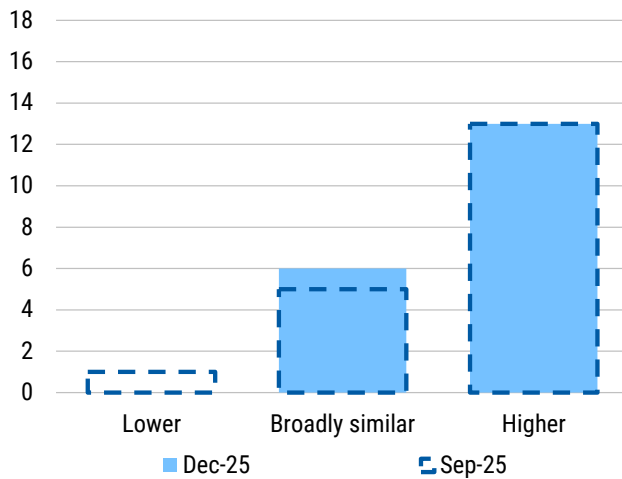
Exhibit 4: December versus September dot plot



Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 5: Uncertainty about GDP growth still elevated

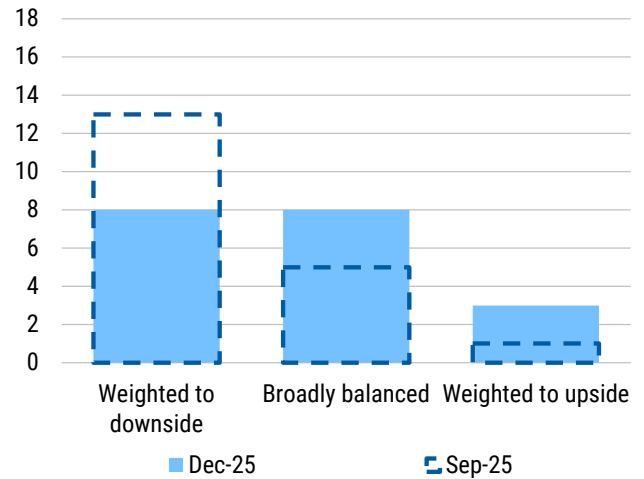
Uncertainty about GDP growth - number of participants



Source: Federal Reserve Board, Morgan Stanley Research

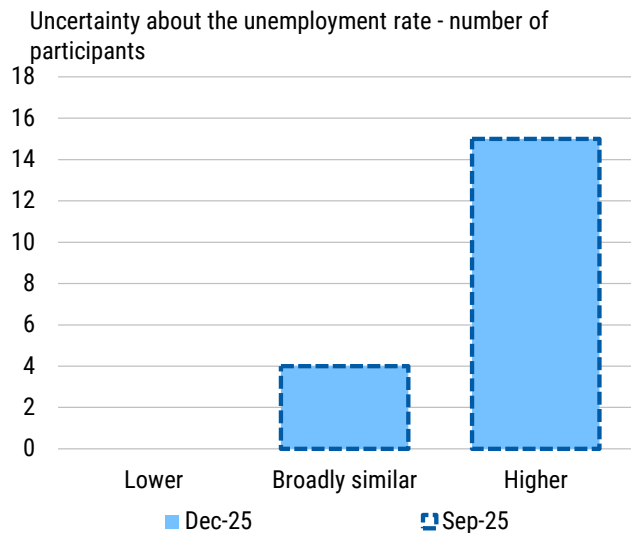
Exhibit 6: With risks to GDP growth skewed to the downside

Risks to GDP growth - number of participants



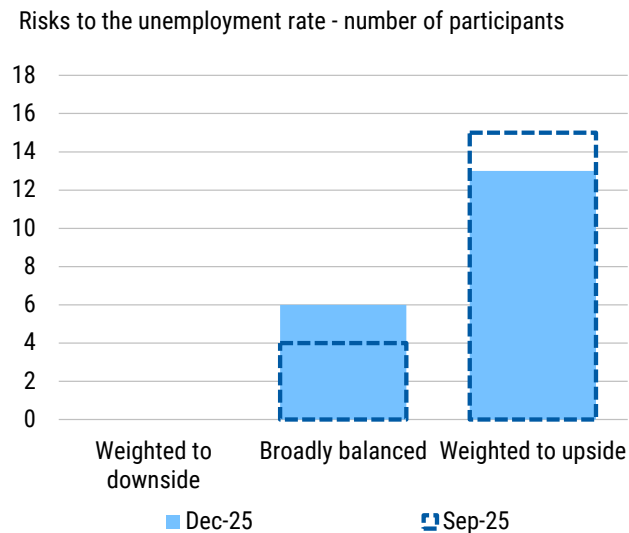
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 7: Uncertainty about the unemployment rate still elevated



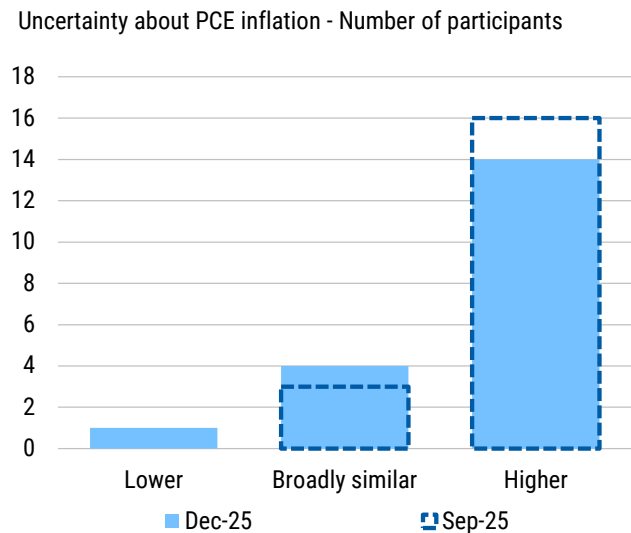
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 8: With risks to the unemployment rate skewed to the upside



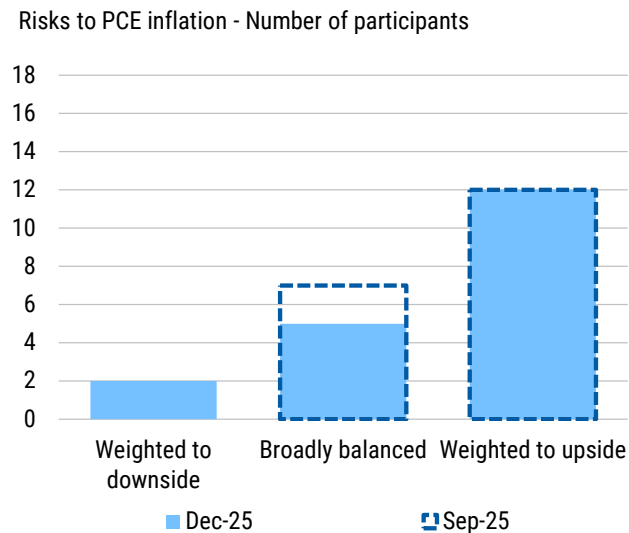
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 9: Uncertainty about inflation still elevated



Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 10: With risks to inflation skewed to the upside



Source: Federal Reserve Board, Morgan Stanley Research

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