MARKETS

Q&A: Fed should be able to manage a soft landing, says analyst

MyWealth Investments CEO says potential headwinds may be US economy not being able to steer clear of recession

BL PREMIUM

12 JANUARY 2024 - 05:00

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Annatjie van Rooyen. Picture: SUPPLIED

The JSE managed to recover some of its earlier losses to end 2023 2% firmer, while the rand trimmed losses for the year as prospects of interest rate cuts by the US Federal Reserve lifted sentiment in December.

However, some Fed officials pushed back on interest rate expectations in 2024, saying it's too early to declare victory over inflation and the Fed is not "pre-committing to cutting interest rates soon and swiftly".

Still, market participants are pricing in the first interest rate cuts as early as March.

Business Day caught up with Annatjie Van Rooyen, CEO of MyWealth Investments, to make sense of what's driving markets.

What are the chances that the Fed will cut rates in 2024, and how soon could that happen?

Fed chair Jerome Powell said in early December the question of when it will be appropriate to cut rates is coming into view.

That welcome dovish tone at the last Fed press conference for the year has resulted in the long-awaited pivot point in the interest rate cycle being discounted by market participants, with the first 25 basis points (bps) cut projected to be implemented at the end of the first quarter of 2024.

The personal consumption expenditure (PCE) index, the Fed's preferred gauge of inflation, has dropped to 3.2% in November 2023 and remains on track to continue moderating to the target of 2% which is fuelling expectations for a total of 75 bps in cuts during 2024 in increments of 25 bps per cut.

So far, economic data has shown the US economy is cooling, but remains resilient. What exactly is the data telling us? What more does the Fed want to see to be comfortable that the fight against inflation is being won? Also, would you say the Fed would be able to manage asoft landing?

Recent indicators suggest that economic growth has slowed and that job gains have moderated but remain strong and that the unemployment rate has remained low.

The US central bank has published new projections for GDP and PCE. GDP growth is expected higher for 2023 (2.6% vs 2.1% in the September projection), but lower in 2024 (1.4% vs 1.5%). PCE inflation was revised lower for both 2023 (2.8% vs 3.3%) and 2024 (2.4% vs 2.5%) as well as core PCE inflation which is seen at 3.2% in 2023 (vs 3.7%) and 2.4% (vs 2.6%) in 2024. Unemployment is expected to remain steady at 3.8% for 2023 and then increase to 4.1% in 2024.

Powell said the US economy might be able to avert recession while inflation came down and that the Fed was unlikely to wait until inflation hits the 2% target to cut rates as it would then be too late.

Interest rates need to be reduced well before inflation reaches the objective of 2% due to the lagged effect of restrictive monetary policy.

The Fed should be able to manage a soft landing based on accurately timed accommodative monetary policy.

Do you think it's reasonable for market participants to expect or price in a rate cut so soon?

Markets are efficient and will always discount present and potential future information at least three months in advance and any unexpected developments are discounted rapidly.

Getting into 2024, what are the potential headwinds that could be at play? Possible tailwinds? Both globally and locally?

Potential tailwinds include the Fed being successful in steering the US economy into a soft landing with accurately timed easing.

Normalisation of demand for goods and services in China is also expected, as is a softening stance in the regulatory space of the tech sector in that country.

There are also likely to be advances on the promising prospects of the AI industry.

Potential headwinds could be the US economy not guaranteed to steer clear of a recession as a result of a lengthy period of tightening.

Locally, economic growth remains a concern as a result of continued weakness in infrastructure development, while political and policy uncertainty in the run-up to the local elections also remain a threat.

Anything else to pay attention to?

It is important to monitor economic data in totality and the subsequent possible deviations from expected monetary policy decisions as central bank action will continue to take centre stage.

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