Fed Rate Meeting: 30 January 2025

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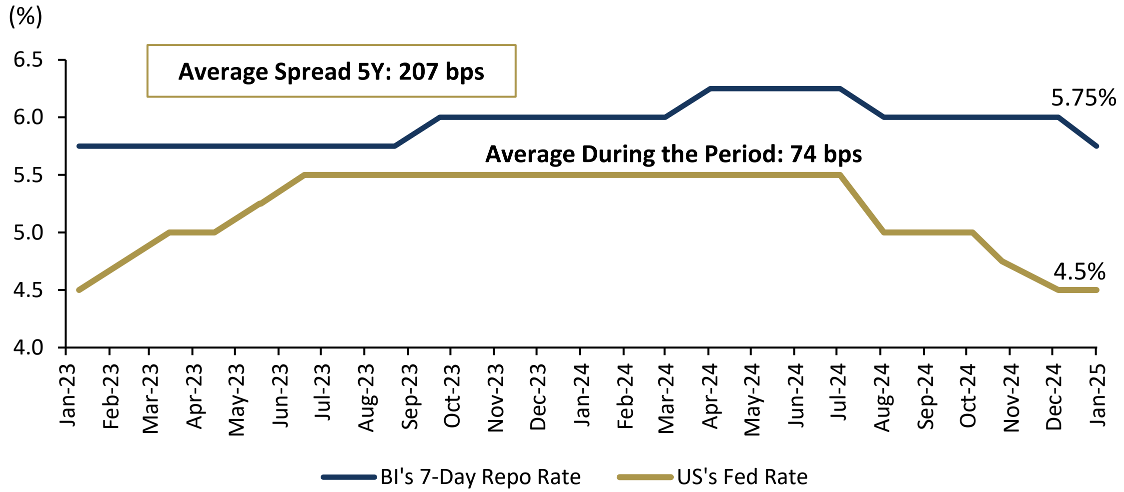
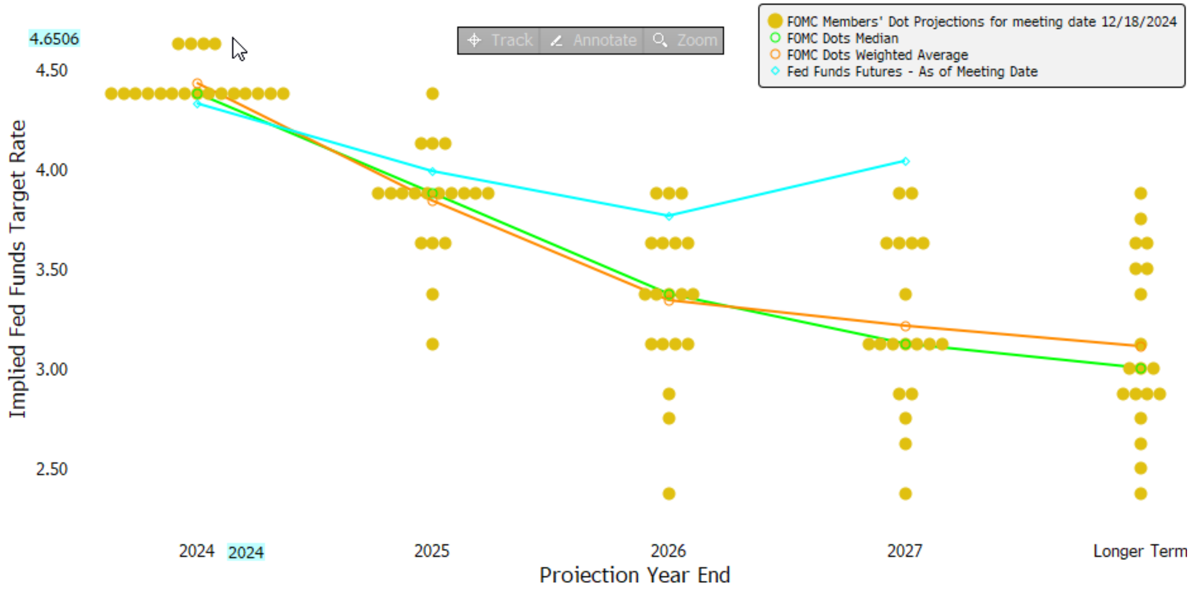
- In-line with our expectation, the Fed's decision to keep its benchmark interest rate at 4.25%-4.5% in its January 2025 meeting reflects a cautious stance amid persistent inflationary risks. After three rate cuts in 2024 totalling 100 basis points, the central bank opted to pause further easing, prioritizing inflation control over premature monetary loosening. Jerome Powell emphasized that further rate cuts are not imminent, as inflation remains above target and the labor market continues to show strength. Notably, the Fed also removed its previous reference to "ongoing progress" toward the 2% inflation target, signalling that price stability remains uncertain.
- U.S. inflation has a high likelihood of experiencing additional pressure, driven by potential widening fiscal deficits, increasing tariffs, and intensifying trade tensions—all of which could prolong the need for restrictive monetary policy stance. This aligns with our projection of the Fed holding rates steady throughout 2025. Given these inflationary risks, the central bank may have limited room to cut rates, possibly maintaining higher-for-longer interest rate policy that could sustain strong U.S. Treasury yields and create capital outflow pressures on emerging markets like Indonesia.
- In contrast to the Fed's cautious stance, Bank Indonesia (BI) took a more proactive approach by unexpectedly cutting its BI 7-Day Reverse Repo Rate by 25 basis points to 5.75% in January 2025. This decision defied market expectations of a hold and underscores BI's focus on stimulating domestic economic growth amid global uncertainty. With Indonesia's foreign exchange reserves at an all-time high of USD 155.7 billion at that time, BI had room to ease monetary policy, aiming to support credit expansion and economic activity. We note that today the USD/IDR has remained relatively unchanged at just below IDR 16,300 level since the cut in BI rate.
- However, BI's dovish stance carries risks. With the Fed likely maintaining higher rates throughout 2025, the narrowing interest rate differential between Indonesia and the U.S. could lead to capital outflows and further depreciation of the IDR. Rising U.S. Treasury yields, fuelled by strong economic data and persistent inflationary pressures, could add further strain on emerging market currencies.
- Overall, the Fed's decision to hold rates steady reinforces a wait-and-see approach to monetary policy, influencing global financial flows and economic strategies, including in Indonesia. For now, policymakers in Jakarta will need to remain vigilant, ensuring that domestic fundamentals remain strong to navigate potential external shocks while sustaining economic momentum into 2025.

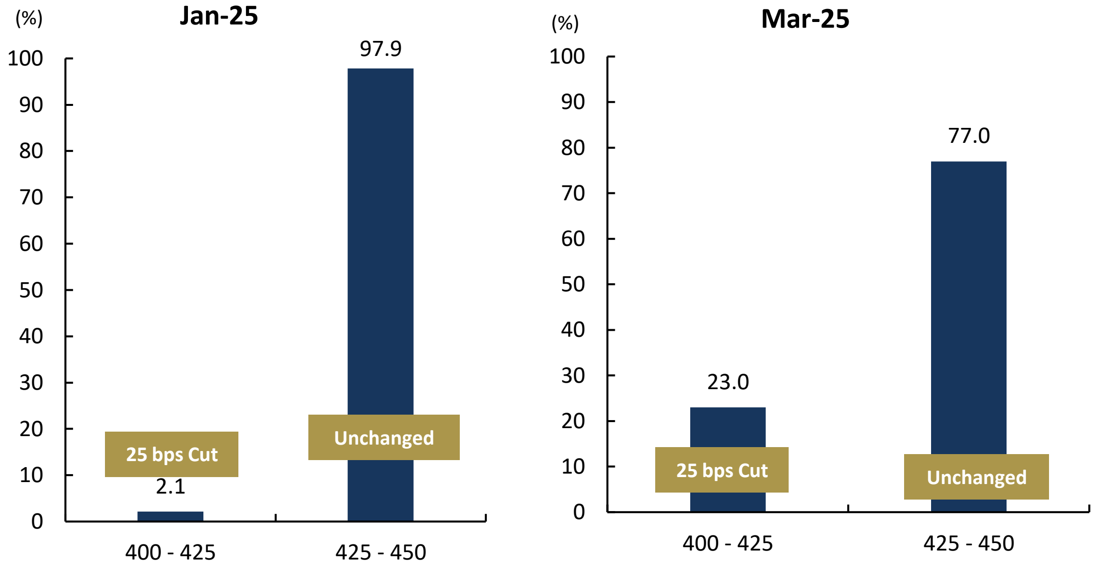
US' Fed Rate and BI's 7-Day Repo Rate



FOMC Dot Plot



Target Rate Probabilities for Jan & Mar-25 Fed Meeting



Sources: Bloomberg, SSI Research

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