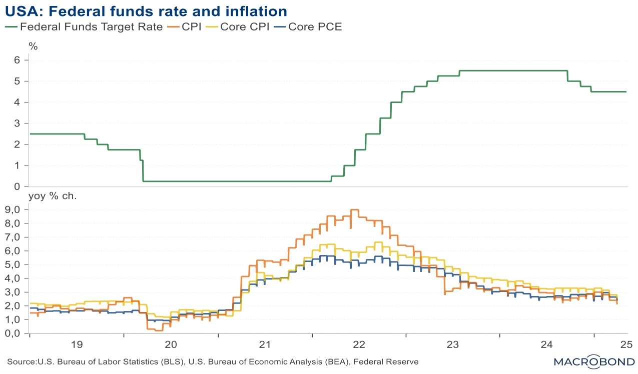
WEEKLY ANALYSIS

NUMBER 902, MAY 12, 2025

Fed continues to delay interest rate cuts

Fed funds rate unchanged, inflation on the decline

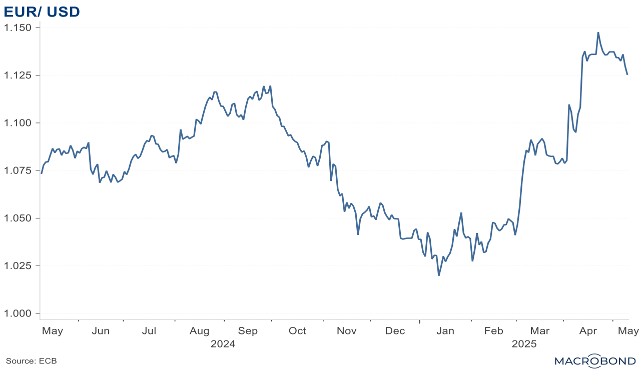
- In line with expectations, at the last week's meeting, the Fed decided to keep interest rates at the existing levels, i.e. the fed funds rate within the target range of 4.25−4.50%, which has been in force since December last year. Inflation in the US in March recorded a decline of -0.1% month-on-month and a decrease to 2.4% year-on-year (+2.8% in February), with core inflation weakening to 2.8%, from 3.1% a month earlier (the core PCE rate fell from 3% to 2.6%). At a press conference, Fed Chairman Powell described inflation as slightly elevated compared to the target of 2%.

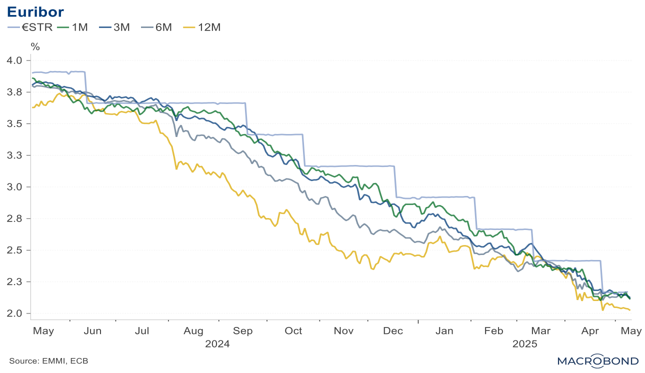


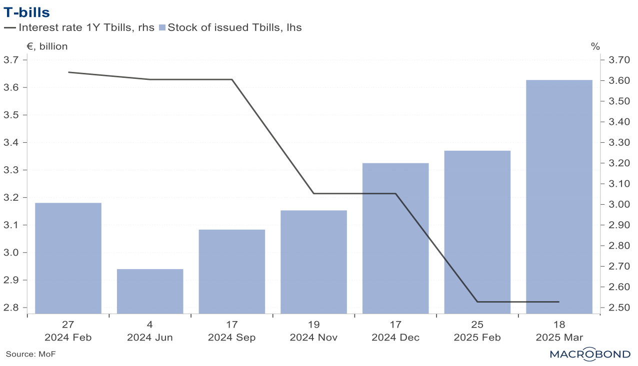
We expect the first reduction of this year in the third quarter

- In the first quarter, US GDP declined by 0.3% quarter-on-quarter (annualized) due to a strong increase in imports ahead of the introduction of tariffs, but domestic demand remained strong, so the Fed assesses that strong growth in economic activity continued with the stabilization of the unemployment rate at low levels and a solid labor market, emphasizing, however, that uncertainty in terms of economic growth continued to grow. Unlike the ECB, the Fed has two goals (the so-called dual mandate) – stable prices and maximum employment. Inflation could follow an unfavourable trend in the period ahead; according to survey indicators, short-term inflation expectations of households and business entities have increased due to the announcement/introduction of tariffs. At the same time, economic growth could slow down and consequently unemployment could rise. Moderating inflation and strengthening growth can be conflicting goals, but as could be read from Powell's address after the meeting, in which he emphasized that "without price stability, we cannot achieve the long periods of strong labor market conditions", the fight against inflation seems to be a priority at the moment. Our estimate is that the Fed will postpone interest rate cuts for the time being, so the first reduction of 25 b.p. could follow in July or only in September, when the effects of tariffs and other measures of the new administration on the economy are clearer, and another cut of 25 b.p. would follow by the end of the year.

- The dollar strengthened after the Fed meeting and the trade deal reached between the US and the UK, so the week ended with an exchange rate of 1.1252 dollars to the euro, down by 0.8% week-on-week.
- Euribor was slightly lowered week-on-week, with 3M and 6M amounting to 2.1% on Friday.
- Crobex maintained its upward trend, rising 2.6% week-on-week, to 3,381 points, owing to the upswing of all sectoral indices (CROBEXindustry +1.6% to 2,527, CROBEXnutris +0.1% to 803, CROBEXtourist +2.8% to 4,423). Crobis rose by 0.1% (to 99.2 points).







LEGAL DISCLAIMER

ECONOMIC RESEARCH
Ivana Jović
Ana Lokin

TRANSLATION
Ana Biloš
Jelena Marinović

www.pbz.hr