MARKETS IN FOCUS

Fed policy insights

March FOMC reaction: Transitory is the base case

March 19, 2025

Key takeaways

- While the U.S. Federal Reserve doesn't see a recession on the horizon, expect that the only certainty is more uncertainty in the near term.
- Federal Open Market Committee members' projections shifted to a significantly more hawkish stance compared with December's forecasts.
- The continuing uncertainty highlights the case for pursuing diversification across asset classes, geographies, sectors, and industries.

There weren't any fireworks yesterday as the Federal Open Market Committee (FOMC) maintained the federal funds target range at between 4.25% and 4.50%, but the market took solace in the fact that the central bank doesn't see a recession on the horizon.

"That's an interesting takeaway because under the surface there are a number of conflicting messages that highlight potential risks to the economy," said Matt Orton, CFA, Chief Market Strategist at Raymond James Investment Management. "Perhaps the market views these different messages as balanced, but I think it just highlights that the only certainty is more uncertainty in the near term."

On the positive side, U.S. Federal Reserve (Fed) Chair Jerome Powell leaned into the idea of "transitory," acknowledging that tariff-induced inflation is likely not here to stay. The dot plot also continued to show that policymakers expect two interest rate reductions this year.[1] It's worth noting, however, that projections shifted to a significantly more hawkish stance compared with December's forecasts – eight participants now see just one or no cuts this year and only two see three cuts. Macroeconomic forecasts were also a bit more stagflationary than expected: growth was marked down to 1.7% this year and 1.8% in the following two years with inflation revised up for 2025. The median estimate for core Personal Consumption Expenditures (PCE) Price Index inflation is now at 2.8%.

"Putting all of this together, the most important takeaway is that the base case remains holding rates steady or perhaps cutting rates should specific macroeconomic thresholds be reached, but hikes are not on the table," Orton said.

[1] Unless otherwise indicated, all data cited is sourced from Bloomberg as of March 19, 2025.

Tariffs and inflation expectations

At the end of the day, Orton said this was an opportunity for the market to formally see how the Fed was thinking about the potential impact of tariffs on the economy. And Powell was finally a bit outspoken on the subject, noting that tariffs are a driving factor in the pickup in inflation expectations. It's clear that the FOMC has serious nonlinear economic worries about tariffs, notably about the potential upside risks to prices and downside risks to growth. Putting all of this together, the Fed is in no hurry to cut rates given all of the uncertainty.

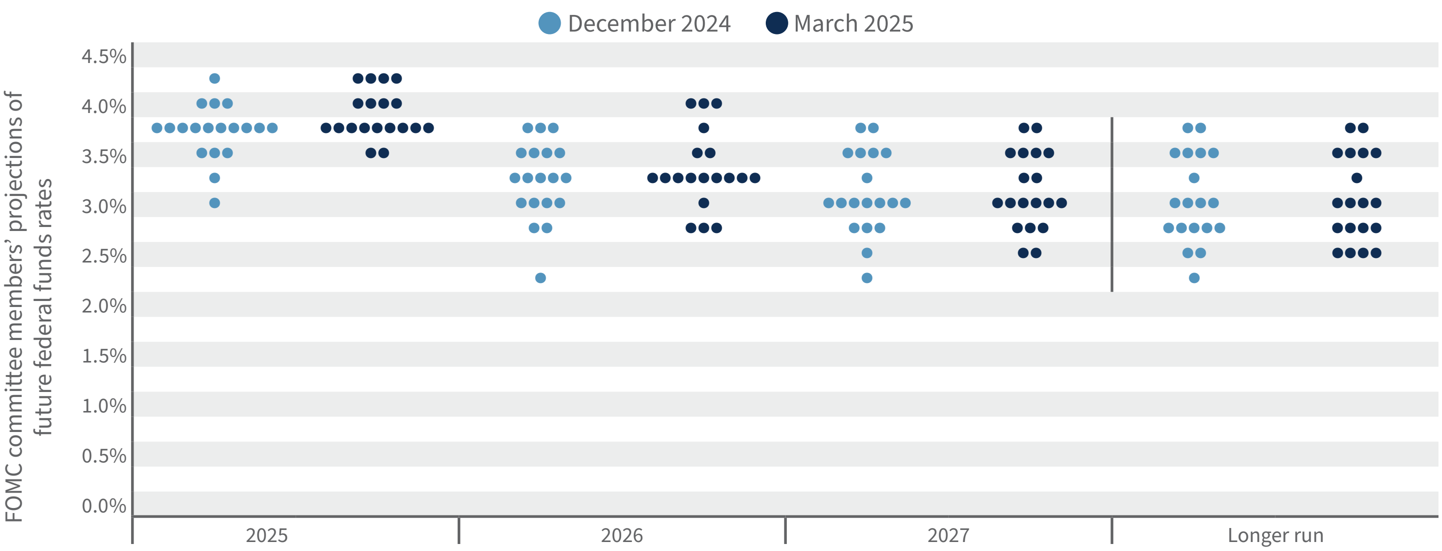
The positive market reaction was encouraging, but a bit extreme considering the lack of a clearly dovish message, Orton said. The relief rally over the past few trading sessions has been expected given extremely oversold conditions, but there hasn't really been any new news on the macro front outside of the FOMC playing down recession concerns. That's certainly positive on the margin, but there is still significant uncertainty even in the Fed's own assessment of the economy and the impact of tariffs.

A time for tactical thinking

"I would avoid chasing the market or buying downside until we get through President Trump's April 2 tariff announcements, which will mean much more to the market than the March FOMC meeting," Orton said. "I actually think there are meaningful risks on April 2 if Trump leverages the notion of reciprocity to penalize anyone and everything he believes to be a trade offender, creating a massive 'shock' to the system that will eventually be negotiated away.

"All of this uncertainty is why I strongly believe in diversification across asset classes, geographies, sectors, and industries," he said. "The need to be tactical is also incredibly important in this environment, but I believe leaning into higher-quality companies, low-beta and away from momentum could serve investors well over the next two weeks."

Federal Open Market Committee past and present dot plots



Source: Bloomberg, U.S. Federal Reserve, as of 3/19/25.

For more market insights and analysis from Raymond James Investment Management, visit **Our Thinking**.

Risk Information:

Investing involves risk, including risk of loss.

Diversification does not ensure a profit or guarantee against loss.

Disclosures:

Index or benchmark performance presented in this document does not reflect the deduction of advisory fees, transaction charges, or other expenses, which would reduce performance. Indexes are unmanaged. It is not possible to invest directly in an index. Any investor who attempts to mimic the performance of an index would incur fees and expenses that would reduce return.

This document is a general communication being provided for informational purposes only. It is educational in nature and not designed to be taken as advice or a recommendation for any specific investment product, strategy, plan feature, or other purpose in any jurisdiction, nor is it a commitment from Raymond James Investment Management or any of its affiliates to participate in any of the transactions mentioned herein. Any examples used are generic, hypothetical, and for illustration purposes only. This material does not contain sufficient information to support an investment decision, and you should not rely on it in evaluating the merits of investing in any securities or products. In addition, users should make an independent assessment of the legal, regulatory, tax, credit, and accounting implications and make their own determinations together with their own professionals in those fields. Any forecasts, figures, opinions, or investment techniques and strategies set out are for information purposes only, based on certain assumptions and current market conditions, and are subject to change without prior notice. All information presented herein is considered to be accurate at the time of production, but no warranty of accuracy is given and no liability in respect of any error or omission is accepted. It should be noted that investment involves risks, the value of investments and the income from them may fluctuate in accordance with market conditions and taxation agreements, and investors may not get back the full amount invested. Both past performance and yields are not reliable indicators of current and future results.

The views and opinions expressed are not necessarily those of the broker/dealer or any affiliates. Nothing discussed or suggested should be construed as permission to supersede or circumvent any broker/dealer policies, procedures, rules, and guidelines.

There are risks associated with dividend investing, including that dividend-issuing companies may choose not to pay a dividend, may not have the ability to pay, or the dividend may be less than what is anticipated. Dividend-issuing companies are subject to interest rate risk and high dividends can sometimes signal that a company is in distress. Dividends are not guaranteed and must be authorized by the company's board of directors.

Sector investments are companies engaged in business related to a specific sector. They are subject to fierce competition and their products and services may be subject to rapid obsolescence. There are additional risks associated with investing in an individual sector, including limited diversification.

Investing in small cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor. The prices of small company stocks may be subject to more volatility than those of large company stocks.

International investing presents specific risks, such as currency fluctuations, differences in financial accounting standards, and potential political and economic instability. These risks are further accentuated in emerging market countries where risks can also include possible economic dependency on revenues from particular commodities or on international aid or development assistance, currency transfer restrictions, and liquidity risks related to lower trading volumes.

Definitions

Beta is a measure of the volatility or systemic risk of a security, group of securities, or portfolio compared with another security, group of securities, portfolio, or the market as a whole.

Core PCE, officially known as the Personal Consumption Expenditures (PCE) excluding Food and Energy, Price Index, is a measure of the prices that U.S. consumers pay for goods and services, not including two categories – food and energy – where prices tend to swing up and down more dramatically and more often than other prices. The core PCE price index, released monthly by the U.S. Department of Commerce Bureau of Economic Analysis, measures inflation trends and is watched closely by the U.S. Federal Reserve as it conducts monetary policy.

The dot plot is a U.S. Federal Reserve chart summarizing the Federal Open Market Committee's (FOMC) outlook for the federal funds rate. Each dot represents the interest rate forecasted by one of the 12 members of the committee.

The federal funds rate is the target interest rate set by the Federal Open Market Committee of the U.S. Federal Reserve. The target is the Fed's suggested rate for commercial banks to borrow and lend their excess reserves to each other overnight.

The Federal Open Market Committee (FOMC) consists of 12 members: the seven members of the Board of Governors of the Federal Reserve System; the president of the Federal Reserve Bank of New York; and four of the remaining 11 Reserve Bank presidents, who serve one-year terms on a rotating basis. The FOMC holds eight regularly scheduled meetings per year at which it reviews economic and financial conditions, determines the appropriate stance of monetary policy, and assesses the risks to its long-run goals of price stability and sustainable economic growth.

Hawkish, dovish, and centrist are terms used to describe the monetary policy preferences of central bankers and others. Hawks prioritize controlling inflation and may favor raising interest rates to reduce it or keep it in check. Doves tend to support maintaining lower interest rates, often in support of stimulating job growth and the economy more generally. Centrists tend to occupy the middle of the continuum between tight (hawkish) and loose (dovish) monetary policy.

Factor investing is an approach to investing that selects securities based on characteristics associated with higher returns. These characteristics, or factors, can be macroeconomic factors or style factors. Macroeconomic factors are focused on broad risks across asset classes and include the rate of inflation: growth in gross domestic product; and the unemployment rate.
Style factors include differences in growth versus value stocks; market capitalization, and industry sector. Factor performance refers to a focus on performance of securities within a particular factor or between groups of different kinds of factors.

Momentum investing is a strategy that aims to capitalize on the continuance of an existing market trend. It is a trading strategy in which investors buy securities that are already rising and look to sell them when they look to have peaked. It entails taking long positions on financial instruments with prices trending up and short positions on instruments with prices trending down.

Nonlinear in finance refers to the relationship between two variables in a possible cause and effect relationship. Linear relationships apply to an independent and dependent variable with a clear and consistent correlation. Nonlinear refers to cases where the correlation is not clear, consistent, or predictable using standard models.

Oversold is a term used to describe a security or group of securities believed to be trading at a level below its or their intrinsic or fair value.

A relief rally is a break from a wider selloff in a market that sees a temporary increase in security prices. Relief rallies can be triggered by news or data that turns out to be better than expected or first believed.

Stagflation, first described after the oil shocks of the 1970s, is an economic condition that includes slow economic growth (or even declines in gross domestic product), relatively high unemployment, and inflation.

Contact us at **800.521.1195** or visit **RJInvestmentManagement.com** for more investment insights.

RAYMOND JAMES | INVESTMENT MANAGEMENT

880 Carillon Parkway, St. Petersburg, FL 33716 | 1.800.521.1195 | RJInvestmentManagement.com