**GS CAS Views: The March FOMC – Goldman's Take from Traders and Research**

**GS CAS Views: The March FOMC – Goldman's Take from Traders and Research**

*All references to "we/us/our" refer to the views and observations of the GS Trading or Research Desks, as noted. All mistakes are my own.*

**TLDR:** Looking forward to tomorrow's FOMC, markets are on the hunt for clarity—whether regarding trade uncertainty, growth estimates, or the possible pause/retirement of QT. GIR expects the FOMC to maintain its cautious stance at the March meeting, signaling that it is not in a hurry to cut interest rates. Looking at the revisions our US team made gives a picture of the difficult balancing act for the FOMC--we took growth down, the unemployment rate up, but inflation also moving higher again back towards 3% on core. That implies pressure on both sides of the Fed's mandate, and makes insurance cuts a tougher proposition than in 2019. We like long front-end US Rates, prefer to short USD in hawkish Fed reactions, and expect credit to track/slightly underrealize its historical beta to stocks as the asset class settles into a new regime.

**GS US Economics Research:**

FOMC to Hold Steady Amid Policy Uncertainty:  The FOMC is expected to maintain its cautious stance at the March meeting, signaling that it is not in a hurry to cut interest rates. Fed officials have emphasized that ongoing policy uncertainty under the new administration and a lack of clarity on the economic outlook justify keeping rates unchanged for now. The rise in tariffs has added to this uncertainty, with inflation and growth forecasts being adjusted accordingly. GIR thinks the FOMC's median economic projections are expected to reflect a 0.3 percentage point increase in 2025 core PCE inflation to 2.8% and a 0.3 percentage point downgrade in 2025 GDP growth to 1.8%. Despite the more challenging outlook, Fed leadership may prefer to maintain the projection of two rate cuts in 2025 to avoid unsettling financial markets.

Tariff Impact Raises Inflation and Lowers Growth Outlook: The increase in tariffs represents a significant shift in the economic landscape, prompting the Fed and market participants to revise their expectations. Higher tariffs are expected to push inflation higher while dampening economic growth, creating a more complicated policy environment for the Fed. Although the normalization cuts projected at the end of 2024 now seem less likely, the Fed may want to keep the 2025 median dot showing two rate cuts to maintain market stability.

GIR believes the rate outlook is expected to remain at 3.875% in 2025, 3.375% in 2026, and 3.125% in 2027, though the average projection could drift higher. The neutral rate projection may also increase slightly to 3.125%, reflecting a higher underlying rate environment. While the Fed acknowledges that inflation remains elevated, it might still consider “insurance cuts” later in the year if the economic risks from tariffs and weaker growth become more pronounced.

Fed Likely to Slow Balance Sheet Runoff: The Fed may address its balance sheet strategy at the March meeting. Fed staff are likely to present options for slowing the pace of balance sheet runoff, with a decision potentially coming as soon as the next meeting in May. The most probable scenario is that the Fed will stop reducing its holdings of Treasury securities while continuing to reduce mortgage-backed securities through the end of the third quarter. However, there is a possibility that both steps could be decided and announced at the March meeting. This adjustment reflects the Fed’s effort to manage liquidity more carefully amid shifting economic and policy conditions. Overall, the Fed’s outlook remains aligned with current market pricing, suggesting that investors are increasingly recognizing the complex trade-offs the Fed faces as it navigates a higher inflation and slower growth environment.

**Table 1:** What’s Priced in the OIS Markets?

| **Dates** | **OIS** | **Cuts Priced In (25bps)** |
|---|---|---|
| 19-Mar-25 | 4.341% | 0.00 |
| 7-May-25 | 4.282% | 0.23 |
| 18-Jun-25 | 4.155% | 0.74 |
| 30-Jul-25 | 4.071% | 1.08 |
| 17-Sep-25 | 3.923% | 1.67 |
| 29-Oct-25 | 3.847% | 1.98 |
| 10-Dec-25 | 3.741% | 2.40 |

*Source: GS Global Markets as of 18Mar25*

Full FOMC preview from GIR *here*

**GS Trading/Strategy**

**Rates:**

- Bullish US Front-End; Bearish Equities; Bullish Swap Spreads: This Fed meeting is going to be about watchful waiting; the Fed is waiting to see how policies play out. DOTs will still show 2 cuts for 2025 and they will drift up in terms of constellation, but median will hold. **Expect weaker string of reports in the March/April data set and Fed will have to cut rates by June.** Likely to be a string of cuts as the Fed will respond to weaknesses in the labor market - **weakness in data will show up in all data by the summer (consumer spending, business sentiment, payrolls, etc.).** Tariffs have implications in opposite directions for the mandate. Key thing is that policy is starting in restrictive place (which is how Powell categorizes it) and given that we are starting from restrictive, I'd conclude they can lower the funds rate as they see labor market weakness arise.

Views: Overall, am bullish US front-end rates as ~60bps of cuts this year offers value and big asymmetry to a growth shock. Bearish US equities near term, buy FX vol as volatility is low for the range of outcomes that can happen, and bullish swap spreads as cash should continue to outperform. *(Thank You Josh Schiffrin – Chief Strategy Officer and Head of Financial Risk for GBM)*

- Neutral on Rate Vol; Slight Bias to be Short on Payer Side: There was a lot of angst going into the data cycle this month amidst the swift repricing in equities and other risk assets. However, the slightly softer payrolls and weaker inflation data we got was not enough to raise a red flag for the Fed, allowing them to sit on the sidelines for the time being until they get more clarity on the Trump administration's tariff agenda**. As a result, vols came down from its extreme levels led by gamma in OTC and exchange as systematic sellers came back to supply the street with gamma on RHS**. Additionally, FM accts sold upper left to fade the higher risk premium that was priced into front end rates**. From here, we're taking a more neutral stance on rate vol, with a slight bias to be short on the payer side via payer ladders and payer ratio trades. However, the rate market will continue to focus on the price action of equities, and a relaxation in that space should bring rate vol lower as well**. *(Thank You Ada Situ – USD Rate Vol Trading)*

- Receive May FOMC: It has been an eventful few weeks leading up to Wednesday's meeting, with front end meeting pricing closely following tariff news and the equity market. Desk had seen better receiving of May FOMC as a cheaper option if recession fears escalate. Last week we saw better paying of meetings with over 15 bps priced-in (ie steepening of May/June and Jul/Sep). As for the meeting itself, we do not expect too many changes to the statement. **There has been some speculation around the dots showing only 1 cut for this year, but our base case is still that the dots show 2 cuts for 2025.** Believe that the Fed will keep the unemployment rate forecast at 4.3%, making it difficult to suggest fewer than 2 cuts despite 2 out of the 8 meetings having passed. We continue to like receiving May FOMC. The risk is that they address the recent tick up in inflation expectations, however, **believe any language on higher inflation will be coupled with the recent softer growth data**. *(Thank You Cemre Ertas – STIR Macro Trading)*

**FX:**

- Short USD in A Hawkish Fed Reaction: – I don't think the Fed will be hawkish, but the market might perceive them as hawkish and **tactically pare back some recent USD weakness**. For example, 1/ if dots rise / fewer cuts for 2025 or 2/ if Inflation expectations rise too much, or if the narrative from Powell or the Q&A suggests that they are more focused on inflation rather than on growth. They likely won't be intentionally hawkish, but if they are perceived to be given the above, we would use this as an opportunity to short USD as the recent narrative shift in Europe is significant and has not played all the way out yet. USD short positioning is not yet stretched. **Further, we would look to fade given the Fed would likely need to walk-back this perceived hawkishness as the eventual growth risks with tariffs materialize.** *(Thank You Alan Stewart – Head of EMEA EM Trading)*

- Fed Constrained on Inflation Side of Mandate: On whether the Fed is able to pivot policy to cushion growth - **the issue for the FOMC is they are somewhat constrained by the inflation side of the mandate-**-core PCE is tracking around 30bps this month, and inflation expectations in the UMich survey will likely give them some pause (though other measures have been better behaved). Looking at the revisions our US team just made gives a picture of the difficult balancing act for the FOMC--we took growth down, the unemployment rate up, but inflation also moving higher again back towards 3% on core. **That implies pressure on both sides of the Fed's mandate, and makes insurance cuts a tougher proposition than in 2019.** *(Thank You Michael Cahill – FX Research)*

**Equities:**

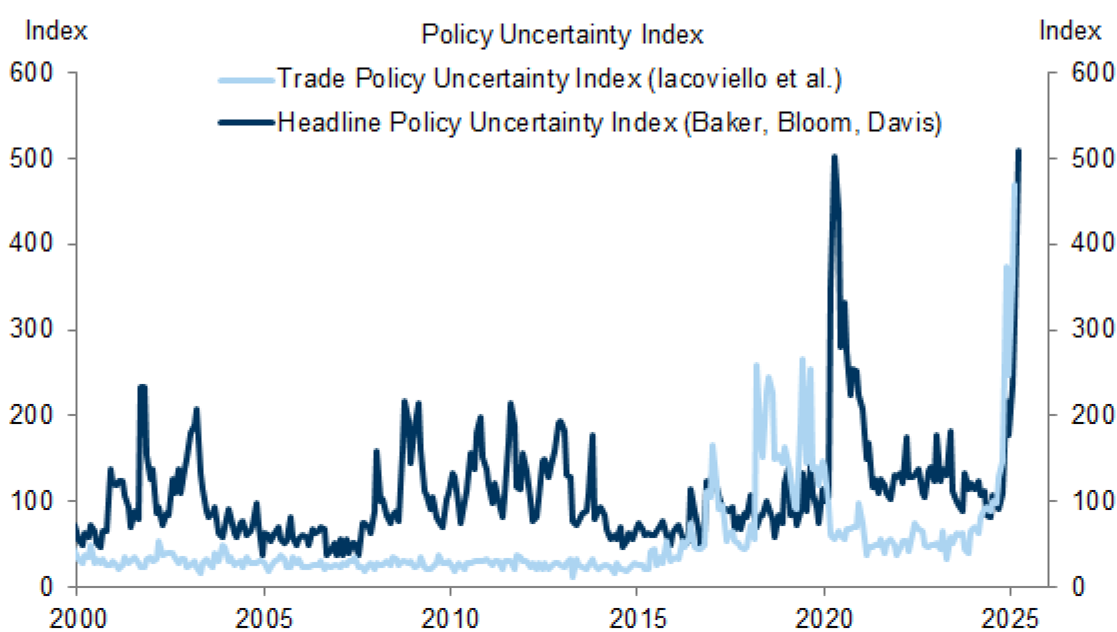
- The Market Isn't Pricing Major Fireworks: Heading into tomorrow's FOMC, the equity vol landscape has changed a bit over the past week. Beginning in late February, vol spiked and skew steepened as trade war concerns sent the SPX tumbling nearly 10**%. After a lighter CPI print last week, the vol market calmed down as spot recovered – 1m vol has come in 5 vols from the highs of late February and skew has relaxed**. While equity vol is still elevated relative to historical levels, we think it's starting to come back into a fair range and the desk has reduced short vol positions. **The SPX implied move for Wednesday is currently around 1.3%. While there certainly is event premium priced in, with the Fed all but certain to maintain their policy rate, the market isn't pricing in any major fireworks**. We think if the event passes with no major news, **this could give continued momentum to the recent relaxation in vol.** *(Thank You Alexis Slattery – Index Deriv Trading)*

- Continue To Favor Diversification Across Equities & Bonds: We expect the Fed to hold the policy rate unchanged, and the market is essentially pricing that too. Two months into the new Administration, focus around policy uncertainty has only increased, and worries about the impact of that are playing a part in the sharp derating of US growth that we have seen recently in markets. With tariffs now a reality, more of the FOMC is likely to incorporate them in the new forecasts, pushing inflation forecasts up and growth forecasts down. A lot will depend on the magnitude of this and the messaging that Chair Powell chooses. **The market reaction is likely to focus around two issues: 1) How worried the Fed sounds about the growth picture**. We think the Fed is unlikely to signal a shift without either sharper data weakness or financial conditions tightening, but the market may be comforted by a clear signal that they will shift quickly if the growth or jobs outlook is deteriorating. With the data not yet meaningfully weaker, how Powell characterizes the recent financial conditions tightening will also be important**. 2) How big a constraint the inflation trajectory – including tariff risks – seems to be playing in postponing easing**. Ultimately, because uncertainty around the path of policy and the economy is what is driving market concerns, and because we think the FOMC will reiterate that it intends to remain on the sidelines until the outlook is clearer, the FOMC meeting may not fully resolve market worries. A shift in the Administration's policies, not the Fed's, would arguably provide a quicker route to a floor under markets. Our growth pricing work suggests that the risks are more balanced going forward—our baseline forecast would now likely create some relief, but risks to growth are to the downside. **We continue to favor diversification across equity markets and between equities and bonds**. If US growth pricing recovers, equities are likely to move higher ahead of a move higher in yields, and US yields have scope to fall if the market further downgrades growth. *(Thank You Dom Wilson & Vickie Chang)*.

**Credit:**

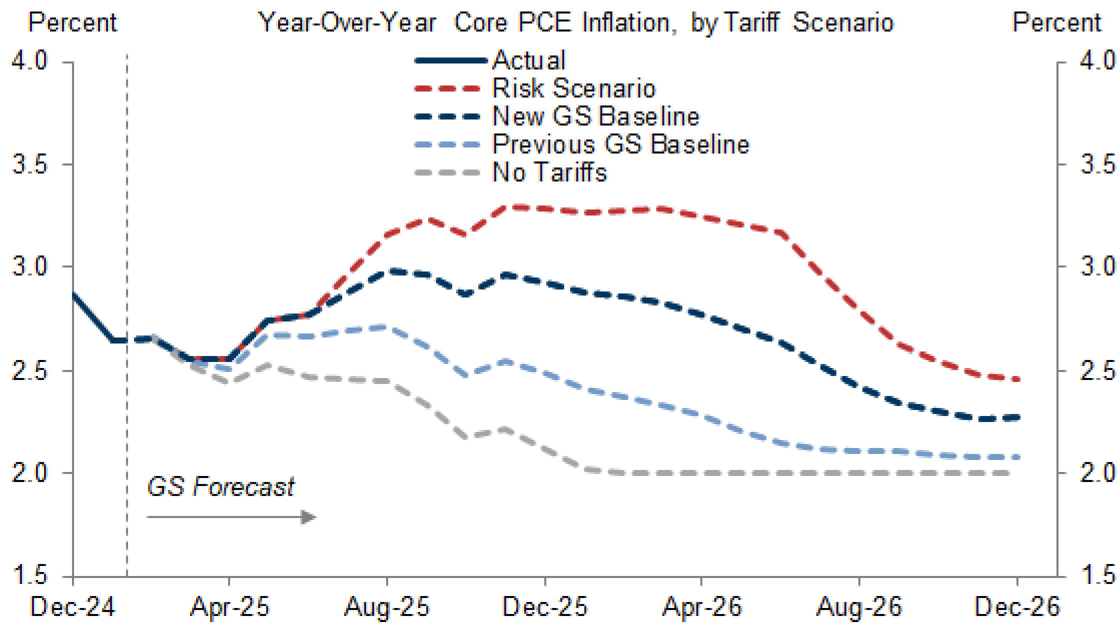
- Credit Has Finally Moved: After a year of trading in a slim realized regime and accounts using the product to source incremental carry, **credit once again started exhibiting its behavior as a fundamental product that repriced wider quickly and picked up down beta vs stocks into the selloff.** Notably, credit vols reracked significantly higher as a function of RM and macro accounts setting fresh hedges on a backdrop of a pullback in vol supply from FM and systematic accounts during the prolonged selloff. Credit curves, traditionally bear steepening in a local selloff and bear flattening in a more global spot down/vol up movement exhibited the latter bias (flattening), while credit tranches saw buyers of risk in higher tiers of the capital structure in a flight to quality trade. In the case of an uneventful Fed, **we expect credit to track/slightly underrealize its historical beta to stocks as the asset class settles in to a new regime**. *(Thank You Manasi Hardikar – Macro Credit Index Trading)*

Exhibit 1: Policy Volatility and Uncertainty Will Keep the FOMC on the Sidelines for Now




Source: Goldman Sachs Global Investment Research, Federal Reserve Board, policyuncertainty.com

Exhibit 2: We Recently Raised Our Tariff Forecast to a 10pp Increase in the Effective Tariff Rate, Which Led Us to Raise Our 2025 Inflation Forecast to Around 3%




Source: Goldman Sachs Global Investment Research

Exhibit 3: The FOMC Statement Will Likely Acknowledge Softer Recent Activity Growth, the Jump in Survey-Based Inflation Expectations, and Greater Uncertainty About the Economic Outlook

Recent indicators suggest that economic activity has continued to expand at a ~~solid~~ moderate pace. The unemployment rate has stabilized at a low level in recent months, and labor market conditions remain solid. Inflation remains somewhat elevated. Although some survey-based measures of longer-term inflation expectations have risen, market-based measures of inflation compensation are little changed.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. The Committee judges that the risks to achieving its employment and inflation goals are roughly in balance. Uncertainty about t~~T~~he economic outlook ~~is uncertain~~has increased, and the Committee is attentive to the risks to both sides of its dual mandate.

Source: Goldman Sachs Global Investment Research

Exhibit 4: The Economic Projections Are Likely to Show Higher Inflation and Lower GDP Growth as Some Participants Pencil in Tariff Effects for the First Time and Others Increase Their Tariff Assumptions

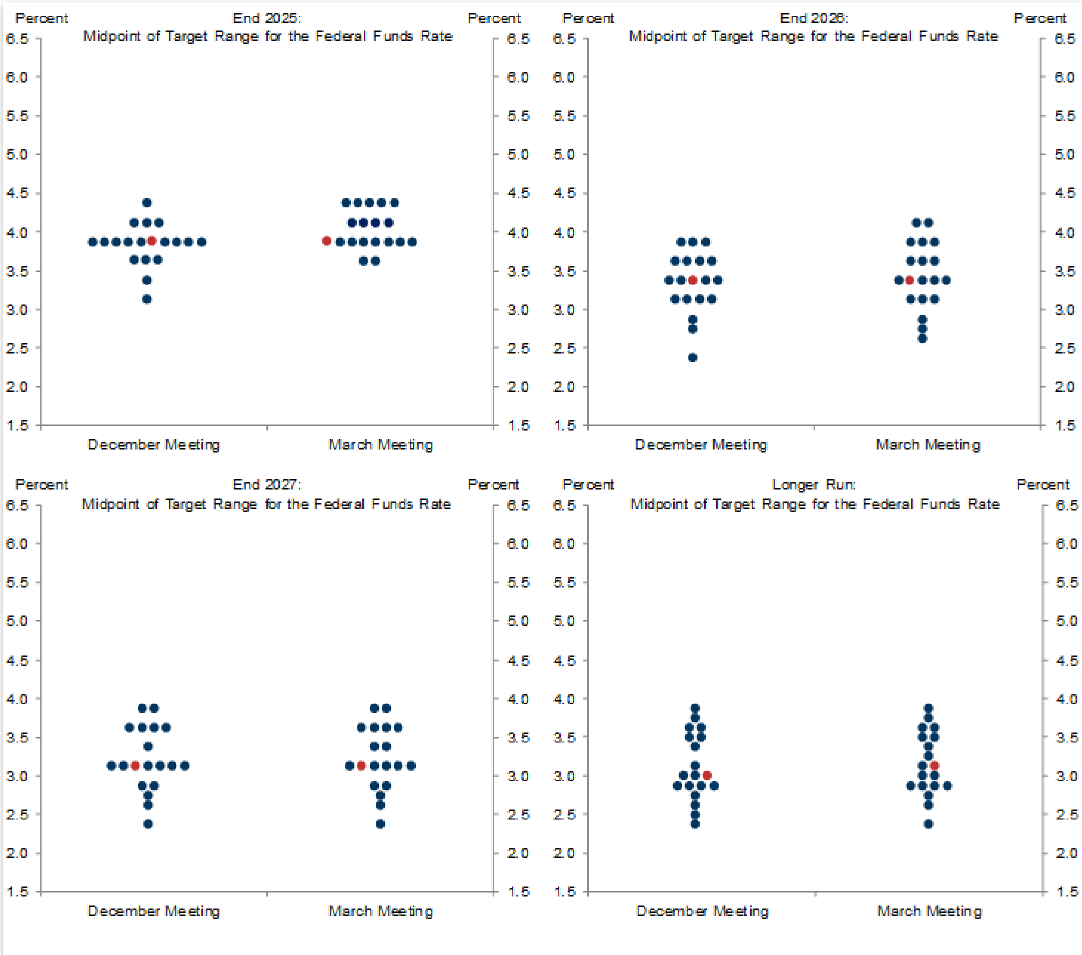
| **Summary of Economic Projections** | **2025** | **2026** | **2027** | **Longer run** |
|---|---|---|---|---|
| **Real GDP Growth*** | | | | |
| *GS Forecast* | *1.7* | *2.0* | *2.1* | |
| **GS Forecast of March SEP** | **1.8** | **1.9** | **1.8** | **1.8** |
| December SEP | 2.1 | 2.0 | 1.9 | 1.8 |
| **Unemployment*** | | | | |
| *GS Forecast* | *4.2* | *4.0* | *3.9* | |
| **GS Forecast of March SEP** | **4.3** | **4.3** | **4.3** | **4.2** |
| December SEP | 4.3 | 4.3 | 4.3 | 4.2 |
| **PCE Inflation*** | | | | |
| *GS Forecast* | *3.0* | *2.3* | *2.0* | |
| **GS Forecast of March SEP** | **2.8** | **2.3** | **2.0** | **2.0** |
| December SEP | 2.5 | 2.1 | 2.0 | 2.0 |
| **Core PCE Inflation*** | | | | |
| *GS Forecast* | *3.0* | *2.3* | *2.0* | |
| **GS Forecast of March SEP** | **2.8** | **2.3** | **2.0** | |
| December SEP | 2.5 | 2.2 | 2.0 | |
| **Fed Funds Rate* (Median)** | | | | |
| *GS Forecast* | *3.875* | *3.625* | *3.625* | |
| **GS Forecast of March SEP** | **3.875** | **3.375** | **3.125** | **3.125** |
| December SEP | 3.875 | 3.375 | 3.125 | 3.000 |
| **Addenda: Fed Funds Rate (Mean)** | | | | |
| **GS Forecast of March SEP** | **4.03** | **3.43** | **3.22** | **3.16** |
| December SEP | 3.84 | 3.34 | 3.21 | 3.11 |

* Data shown are medians.

Note: GDP growth and inflation forecasts are Q4/Q4. Unemployment is the Q4 average. The funds rate is the level at the end of the year.

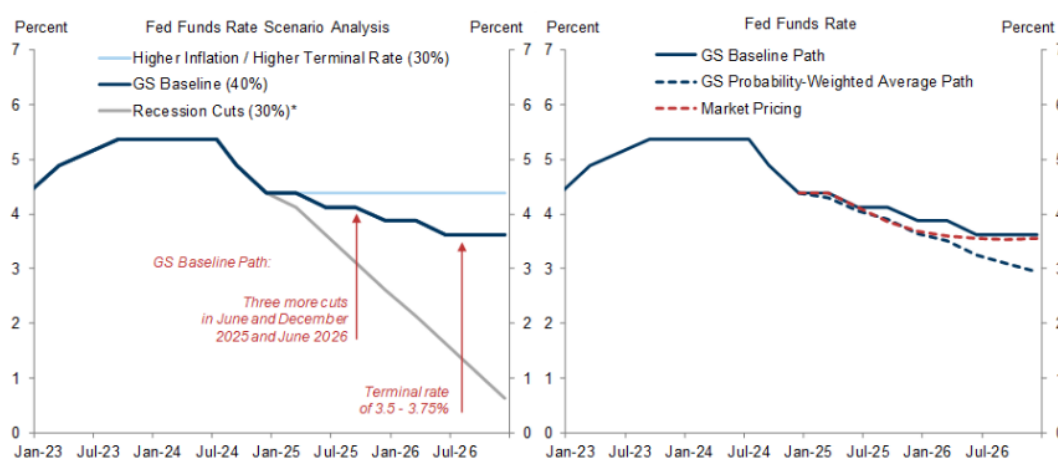
Source: Goldman Sachs Global Investment Research, Federal Reserve Board

Exhibit 5: The Fed Leadership Might Prefer for the Dots to Continue to Show Two Cuts This Year To Avoid Adding to Recent Market Turbulence, Even Though Normalization Cuts Now Look Further Off




Source: Goldman Sachs Global Investment Research

Exhibit 6: Market Pricing Overlaps Closely With Our Probability-Weighted Fed Forecast Over the Next Year




*This is the probability of a recession happening at any point over the horizon shown above. Our 12-month recession probability is 20%.

Source: Goldman Sachs Global Investment Research

"Simulated results are for illustrative purposes only. GS provides no assurance or guarantee that the strategy will operate or would have operated in the past in a manner consistent with the above analysis. Past performance figures are not a reliable indicator of future results."