CURRENCIES

Yen rallies after Federal Reserve signals rate cuts in 2024

Market watchers shift focus to BOJ for more signs of policy shift

The Fed's decision to hold interest steady in December was expected, but the bigger potential for rate cuts next year moved markets. © Reuters

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NEW YORK -- The Federal Reserve held interest rates steady at a 22-year high on Wednesday but signaled that cuts of up to 75 basis points would be coming in 2024.

Wall Street was expecting the Fed's decision to stand pat, but new forecasts from central bank officials showed a turn from the hawkish rate environment Fed Chairman Jerome Powell had indicated as recently as this month.

That bolstered Japan's currency, which strengthened to as much as 142.6 yen to the dollar, for a gain of more than 3 yen from the close of the Tokyo market.

Wednesday marked the yen's biggest move against the dollar since a **rally last week** following Bank of Japan Gov. Kazuo Ueda's comments that were seen as laying the groundwork for an end to the BOJ's negative interest rate policy.

"I think there's more room for the yen but it's going to need another catalyst here," said Amarjit Sahota, executive director of foreign exchange advisory firm Klarity FX.

Sahota said he expects to see more yen strength ahead, in part due to lower U.S. interest rates, but also because of more confidence that the BOJ is finally serious about moving away from negative rates.

"This time [the markets] feel like they've got something more to sink their teeth into," he said.

Meanwhile, the U.S. dollar index dropped at one point to 102.78, its lowest level since Nov. 28, on Fed officials' updated outlook. Seventeen of the 19 officials project the federal funds rate to be lower at the end of next year than the current 5.25% to 5.50% range that has stood in place since the last rate hike in July.

U.S. stocks soared, with gains of about 1.4% for the S&P 500, the Dow Jones Industrial Average and the Nasdaq. The Dow closed above 37,000 for the first time. U.S. 10-year bond yields were at their lowest since July, and two-year yields -- which are sensitive to policy rate expectations -- at their lowest since the regional banking crisis in March.

This week's Fed meeting follows recent U.S. economic data showing inflation remained in check as well as a strong jobs report.

"Inflation has eased from its highs, and this has come without a significant increase in unemployment. That's very good news," Powell said following the Fed decision. "But inflation is still too high, ongoing progress in bringing it down is not assured and the path forward is uncertain."

Powell said the Fed wasn't ruling out more rate hikes but signaled that it was likely at or near its peak in this tightening cycle. Fed officials "do not view it as likely to be appropriate to raise interest rates further, neither do they want to take the possibility off the table."

As far as the timing of the first rate cut, Klarity's Sahota said unless there's a surprise in data showing a significant decline in consumer sentiment or manufacturing activity, he wouldn't expect any tightening until May.

"But once they come, there's nothing stopping them from slamming down pretty quickly, like a 25 [basis point cut] in two consecutive months," he said.