

US economy : FOMC November meeting

Uncertainties in policy, outlook & rate cut path

Key message

1. The November FOMC meeting deleted the wording, “Confidence in inflation returning to target” in its statement, indicating the Fed has begun discussing the risk of inflation fueled by Trump’s economic policies.
2. The labor market is no longer tight. So the Fed removed its remark regarding employment growth slowdown, stating the labor market has eased instead.
3. The Fed hinted rate cuts will slow. We predict a rate cut of 25bps in December and 1Q25F, respectively, and that rate reductions from 2Q25F onwards will depend on economic and fiscal policies.
4. Medium- and long-term Treasury yields have surged, reflecting a slowdown in rate cuts and the negatives of the Trump presidential election victory. We recommend slightly increasing medium- and long-term bond holdings.
5. Treasury issuance will grow on the US fiscal deficit. The pickup in the term premium on 10-year bonds will boost 10-year yield to over 5.0%.

Event

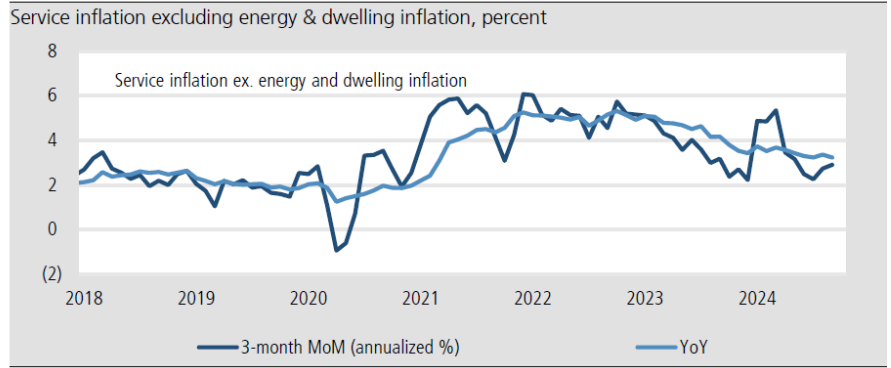
The Fed reduced the federal funds rate from 4.75-5.0% to 4.5-4.75% at the November FOMC meeting, in line with consensus. The post-meeting statement reiterated the risks of attaining the employment and inflation goals are in balance, while removing the wording of “Confidence in inflation returning to target”. Remarks regarding a slowdown in employment growth were also deleted, stating the labor market has eased instead.

Analysis

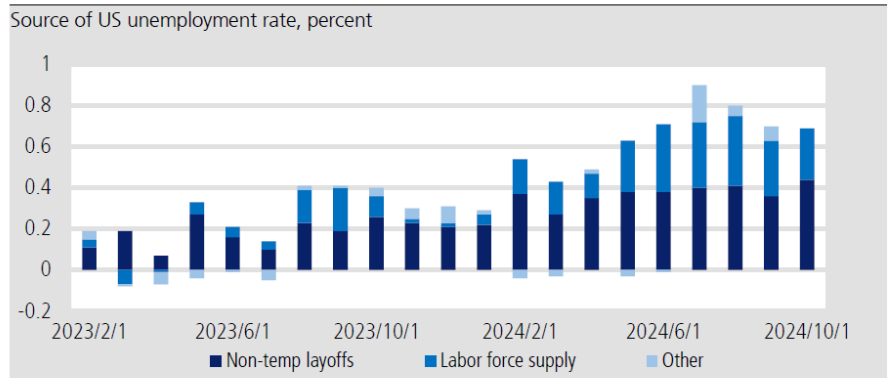
- (1) Recent inflation data indicate core service inflation is cooling off at a slower pace and could pick up in the near term (Figure 1). Also, the risk of higher inflation will be fueled by the Trump presidency and Republican control of both chambers of Congress, as well as policies of immigrant deportation, higher tariffs and domestic tax reductions. While Fed Chair Powell said at the post-meeting press conference that Fed policies have not taken into account potential fiscal policy changes, pending congressional approval of relevant laws, the deletion of “Confidence in inflation returning to target” in the post-meeting statement shows that the Fed has begun discussing related risks.
- (2) Recent labor market data have been uneven, with nonfarm payroll growth fluctuating widely and actual data being much higher than advance estimates. This, combined with the Boeing (US) strike and the effect of two hurricanes, has sent confusing signals about changes to the labor market. That said, other relevant data indicate the overall labor market is no longer tight. The Fed thus signaled a possible slower rate cut path.
- (3) There is no recession risk in the labor market. However, the unemployment rate caused by non-temp layoffs is creeping up (Figure 2). This is why the Fed will continue to ease interest rate restrictiveness. Policy rate restrictiveness has dropped from 160bps in September to 85bps (Figure 3). We forecast there is a 80% probability, higher than consensus of 67%, that the Fed will reduce policy rates by 25bps in December to 4.25-4.5%, for lower restrictiveness of 60bps. We predict the Fed will cut rates by another 25bps in 1Q25F, resulting in a federal funds rate of 4.0-4.25%. We believe the Fed will ease the speed and magnitude of rate cuts from 2Q25F onwards to avoid the risk of overly aggressive rate reductions by also considering changes to US fiscal policy. We expect the Fed will stop cutting rates after shaving off another 25bps when the benchmark interest rate decreases to 3.75-4.0%.

Conclusion

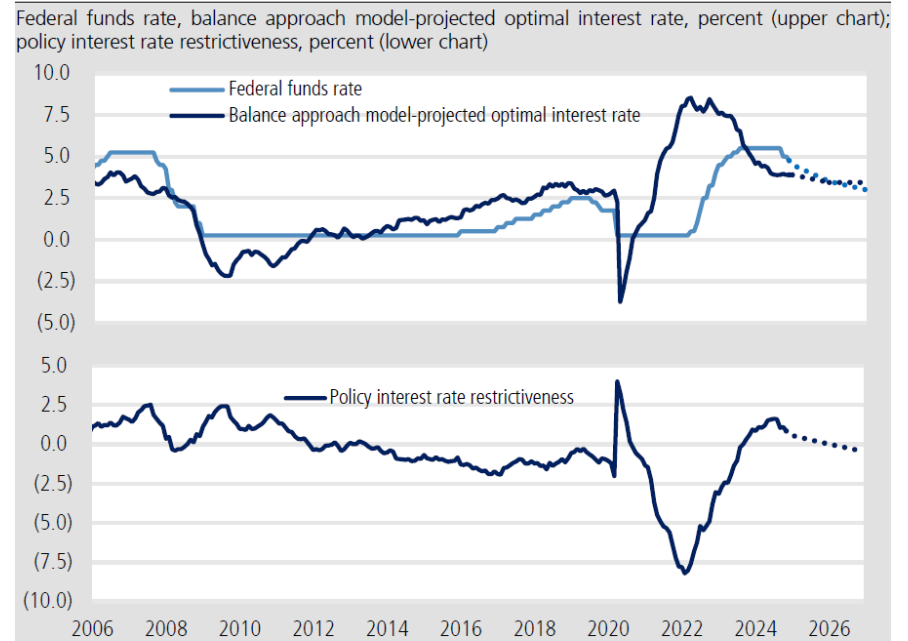
- (1) The current policy interest rate range is 4.5-4.75%, the short-term ceiling of the 10-year bond yield. The extent of rate cuts over the next 12 months has narrowed to 75-100bps (Figure 4). With medium- and long-term bond yields having rebounded significantly, reflecting an economic soft landing and less room for rate cuts, further yield rises will be limited, especially now that Trump’s winning the White House bodes ill for Treasury notes. As rate reductions and economic growth slow gradually in the future, we forecast the 10-year bond yield will return to 3.8-4.2%. We recommend engaging medium- and long-term Treasury bonds.
- (2) We will monitor the risk of overly rapid supply of Treasuries spurred by the US fiscal deficit (Figure 5). The term premium on 10-year bonds could pick up to 100-150bps (Figure 6), pushing the 10-year Treasury yield back up to over 5%.

Figure 1: Core service inflation cooling off at a slower pace


Source: Bloomberg, KGI Research

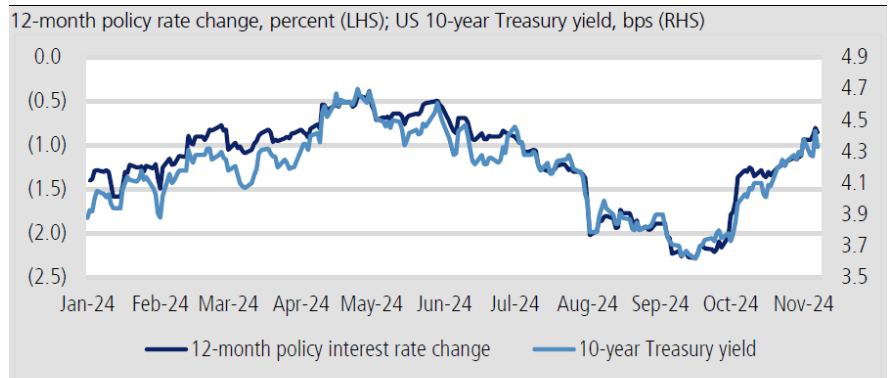
Figure 2: Unemployment rate caused by non-temp layoffs rising


Source: Bloomberg, KGI Research

Figure 3: Policy interest rate restrictiveness down from 160bps in September to 85bps


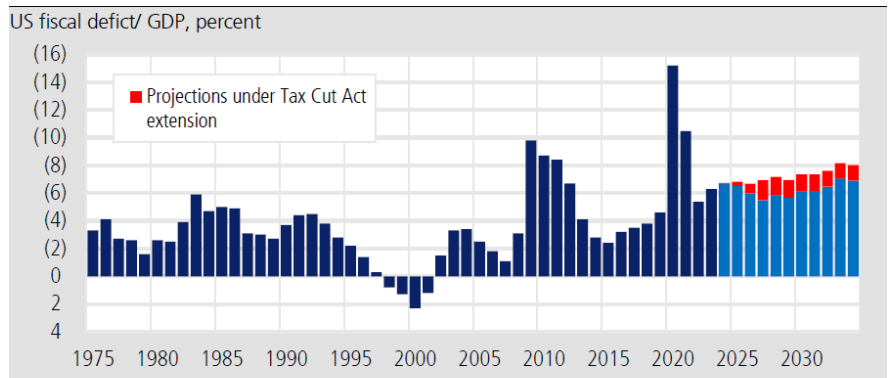
Source: Bloomberg, KGI Research

Figure 4: Policy interest rate at short-term ceiling of 10-year bond yield, narrowing rate cuts to 75-100bps over next 12 months



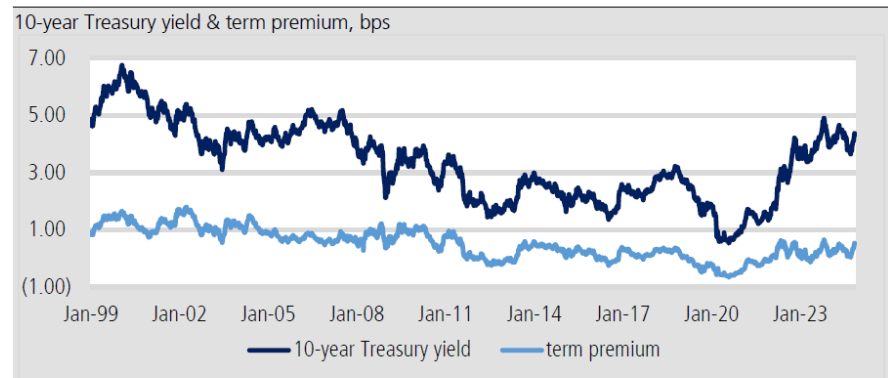
Source: Bloomberg; KGI Research

Figure 5: Rising US fiscal deficit leads to overly-fast Treasuries supply



Source: Bloomberg; KGI Research

Figure 6: 10-year bond term premium likely to rebound to 100-150bps



Source: Bloomberg; KGI Research

Figure 7: Key US economic data

Indicators		Units	2020	2021	2022	2023	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	Apr-24	May-24	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24
GDP	GDP QoQ SAAR	QoQ %, SAAR					3.2			1.6			3.0			2.8		
	GDP YoY	YoY %	(2.2)	6.1	2.5	2.9	3.2			2.9			3.0			2.7		
Consumer prices	CPI	YoY %	1.2	4.7	8.0	4.1	3.1	3.4	3.1	3.2	3.5	3.4	3.3	3.0	2.9	2.5	2.4	
	Core CPI	YoY %	1.7	3.6	6.2	4.8	4.0	3.9	3.9	3.8	3.8	3.6	3.4	3.3	3.2	3.2	3.3	
	PCE price index	YoY %	1.1	4.1	6.6	3.8	2.7	2.7	2.6	2.6	2.8	2.7	2.6	2.4	2.5	2.3	2.1	
	Core PCE index	YoY %	1.3	3.6	5.4	4.2	3.2	3.0	3.1	2.9	3.0	2.9	2.7	2.6	2.7	2.7	2.7	
Labor market	Labor force participation rate	%	61.5	62.0	62.3	62.5	62.8	62.5	62.5	62.5	62.7	62.7	62.5	62.6	62.7	62.7	62.7	62.6
	Unemployment rate	%	8.1	5.4	3.6	3.6	3.7	3.7	3.7	3.9	3.8	3.9	4.0	4.1	4.3	4.2	4.1	4.1
	Non farm payrolls	'000	(9,274)	7,245	4,528	3,013	182	290	256	236	310	108	216	118	144	78	223	12
	Net Change In total employment in labor force	'000	(8,856)	6,135	4,528	3,013	586	(683)	(31)	(184)	498	25	(408)	116	67	168	430	(368)
	Challenger job cut announce	YoY %	15.8	(1.2)	(1.7)	2.1	(41)	(20)	(20)	9	1	(3)	(20)	20	9	1	53	51
	Opening/ hiring	x	1.07	1.56	1.75	1.58	1.60	1.54	1.54	1.52	1.49	1.41	1.46	1.51	1.42	1.45	1.34	
	Avg. hourly earnings	YoY %	5.4	5.0	4.9	4.3	4.3	4.3	4.4	4.3	4.1	3.9	4.0	3.8	3.6	3.9	3.9	4.0
Economic activity & business condition	Industrial production	YoY %	(7.1)	4.4	3.4	0.2	(0.2)	0.8	(1.2)	(0.1)	(0.3)	(0.8)	0.1	0.8	(0.5)	(0.2)	(0.6)	
	Durable goods orders	YoY %	(4.6)	18.4	8.2	4.4	10.0	3.4	(0.9)	4.5	(2.2)	1.2	(1.4)	(11.3)	2.8	(0.4)	(2.8)	
	Core capital goods orders	YoY %	(8.3)	12.8	6.5	1.7	1.4	0.8	(0.2)	3.2	(0.9)	2.8	(0.5)	(2.2)	2.0	(1.5)	0.7	
	Total business inventory/ sales ratio	x	1.44	1.28	1.34	1.37	1.36	1.37	1.38	1.37	1.37	1.37	1.38	1.38	1.37	1.38		
	Manufacturing inventory/ sales ratio	x	1.62	1.49	1.47	1.48	1.48	1.48	1.49	1.47	1.47	1.46	1.47	1.46	1.45	1.46	1.46	
	Retail inventory/ sales ratio	x	1.34	1.15	1.24	1.27	1.28	1.28	1.30	1.29	1.29	1.30	1.31	1.33	1.32	1.33		
	ISM manufacturing index	Point	52.4	60.6	53.5	47.1	46.6	47.1	49.1	47.8	50.3	49.2	48.7	48.5	46.8	47.2	47.2	46.5
	ISM non-manufacturing index	Point	54.3	62.4	56.1	52.8	52.5	50.5	53.4	52.6	51.4	49.4	53.8	48.8	51.4	51.5	54.9	56.0
	ISM manufacturing index: new orders	Point	53.9	64.3	51.6	46.0	47.8	47.0	52.5	49.2	51.4	49.1	45.4	49.3	47.4	44.6	46.1	47.1
	Chicago Fed National activity Index	Point	(0.46)	0.38	(0.01)	(0.11)	0.21	(0.11)	(0.81)	0.39	(0.15)	(0.39)	0.18	(0.15)	(0.26)	(0.01)	(0.28)	
	Conference board leading index	YoY %	(4.7)	7.1	0.4	(7.7)	(7.6)	(7.1)	(7.1)	(6.5)	(5.5)	(5.5)	(5.2)	(4.9)	(5.1)	(5.0)	(4.8)	
	C&I Loans for large/medium - tightening lending standard	%	37.6	(15.1)	11.8	43.9			14.5			15.6			7.9			
C&I Loans for large/medium - stronger demand	%	(15.5)	(1.2)	12.4	(42.3)			(25.0)			(26.6)			0.0				
Housing market	Building Permits	'000, SAAR	1,478	1,738	1,682	1,518	1,508	1,530	1,508	1,563	1,485	1,440	1,399	1,454	1,406	1,470	1,428	
	Housing starts	'000, SAAR	1394	1,605	1,552	1,421	1,510	1,568	1,376	1,546	1,299	1,377	1,315	1,329	1,262	1,361	1,354	
	New home sales	'000, SAAR	831	770	637	666	611	654	664	643	683	736	672	672	726	709	738	
	Existing home sales	mn, SAAR	5.6	6.1	5.1	4.1	3.9	3.9	4.0	4.4	4.2	4.1	4.1	3.9	4.0	3.9	3.8	
	NAHB housing market index	Point, SA	70	81	59	44	34	37	44	48	51	51	45	43	41	39	41	43
	S&P/Case-Shiller 20-city composite home price index	YoY %	10.4	18.7	4.9	6.4	5.6	6.4	6.8	7.5	7.5	7.2	6.8	6.5	5.9	5.2		
Consumption	Personal expenditures	YoY %, SA	(2.5)	8.8	3.0	2.5	3.1	3.6	1.9	2.1	2.7	2.4	2.8	2.9	2.8	3.0	3.1	
	Retail sales	YoY %	0.8	18.2	9.1	3.6	4.0	5.5	0.3	2.1	3.6	2.8	2.6	2.0	2.9	2.2	1.7	
	Retail sales ex-autos	YoY %	1.5	17.3	10.6	3.5	3.6	4.6	0.9	2.0	3.7	3.2	2.9	3.3	3.2	2.5	2.2	
	Domestic vehicles sales	mn, SA	173.0	179.2	164.8	185.2	15.3	15.8	15.0	15.8	15.5	15.7	15.9	15.3	15.8	15.1	15.8	16.0
	Conference board consumer confidence	Point	101.0	112.7	104.5	105.4	101.0	108.0	110.9	104.8	103.1	97.5	101.3	97.8	101.9	105.6	99.2	108.7
	Michigan Consumer Sentiment Index	Point	81.5	77.6	59.0	65.4	61.3	69.7	79.0	76.9	79.4	77.2	69.1	68.2	66.4	67.9	70.1	70.5
Fiscal	Budget balance	As % of GDP	(15.2)	(10.5)	(5.4)	(6.5)	(6.3)	(6.5)	(6.3)	(6.4)	(5.9)	(5.7)	(6.1)	(5.6)	(5.6)	(7.2)	(6.3)	
	Current account balance	As % of GDP	(2.8)	(3.7)	(3.9)	(3.3)	(3.2)	(3.2)	(3.2)	(3.2)	(3.2)	(3.2)	(3.2)	(3.3)	(3.3)			
Int'l balance	Net foreign securities transactions	US \$bn	505	907	1,321	932	101.1	88.2	(69.4)	25.6	58.6	1.8	(42.8)	80.5	137.9	111.4		
	Federal funds rate	%	0.25	0.25	4.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.50	5.00	5.00	
Monetary & financial	10-Year treasury yield	%	0.91	1.51	3.87	3.88	4.33	3.88	3.91	4.25	4.20	4.68	4.50	4.40	4.03	3.90	3.78	4.28
	Dollar index	Point	89.9	95.7	103.5	101.3	103.5	101.3	103.3	104.2	104.5	106.2	104.7	105.9	104.1	101.7	100.8	104.0

Source: Bloomberg; KGI Research

Figure 8: Key Taiwan economic data

Indicators		Units	2020	2021	2022	2023	Nov-23	Dec-23	Jan-24	Feb-24	Mar-24	Apr-24	May-24	Jun-24	Jul-24	Aug-24	Sep-24	Oct-24		
GDP	GDP YoY	YoY %	3.4	6.6	2.6	1.3	4.8				6.6				5.1				4.0	
Consumer prices	CPI	YoY %	(0.2)	2.0	3.0	2.5	2.9	2.7	1.8	3.1	2.2	1.9	2.2	2.4	2.5	2.4	1.8	1.7		
	Core CPI	YoY %	0.7	1.9	2.7	2.4	2.4	2.4	1.7	2.9	2.1	1.8	1.8	1.8	1.9	1.8	1.8	1.6		
Labor market	Unemployment rate	%	3.8	3.7	3.6	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.3	3.3	3.4	3.4			
Economic activity	Industrial production	YoY %	8.8	14.7	(1.7)	(12.5)	(1.8)	(3.8)	15.6	(1.3)	4.2	14.5	15.7	12.8	13.0	12.5	11.2			
	Markit Taiwan manufacturing PMI	Point			47.7	46.3	48.3	47.1	48.8	48.6	49.3	50.2	50.9	53.2	52.9	51.5	50.8	50.2		
	NDC monitoring light signal						Yellow-blue	Yellow-blue	Green	Green	Green	Yellow-red	Yellow-red	Red	Yellow-red	Red	Yellow-red			
	NDC monitoring indicators	Point	24.3	39.0	24.2	14.4	20.0	22.0	27.0	29.0	31.0	35.0	36.0	38.0	35.0	39.0	34.0			
	NDC composite leading index	YoY %	(0.4)	4.7	(3.1)	(1.5)	(1.8)	(1.9)	(2.0)	(1.8)	(1.2)	(0.2)	1.0	2.0	2.7	3.3	3.6			
	NDC composite coincident index	YoY %	(0.9)	8.2	(1.4)	(8.1)	(1.9)	0.0	1.9	3.6	5.2	6.5	7.6	8.3	8.6	8.8	9.0			
Consumption	Retail sales	YoY %	0.2	3.3	7.4	9.7	12.0	4.5	3.5	12.3	5.7	1.6	2.6	3.9	3.1	1.1	3.2			
Trade	Exports	US\$bn	345.2	446.6	479.7	432.6	37.5	39.9	37.2	31.4	41.8	37.5	37.4	39.9	39.9	43.6	40.6			
	Imports	US\$bn	285.8	381.3	428.1	352.1	27.7	28.8	34.7	23.6	33.1	31.0	31.3	35.2	35.1	32.1	33.5			
	Trade balance	US\$bn	59.4	65.3	51.6	80.5	9.8	11.1	2.5	7.9	8.7	6.5	6.1	4.7	4.8	11.5	7.1			
	Export growth	YoY %	4.9	29.4	7.4	(9.8)	3.7	11.7	17.7	1.3	18.8	4.3	3.4	23.4	3.1	16.8	4.5			
	Import growth	YoY %	0.1	33.4	12.3	(17.8)	(14.8)	(6.7)	18.7	(17.8)	7.2	6.5	0.6	33.9	15.8	11.7	17.3			
	Export orders	US\$bn	533.7	674.1	666.8	561.0	50.6	43.8	48.4	37.7	47.2	47.1	48.9	45.6	50.0	50.2	53.8			
	Export order growth	YoY %	10.1	26.3	(1.1)	(15.9)	1.0	(16.0)	1.9	(10.4)	1.2	10.8	7.0	3.1	4.8	9.1	4.6			
Monetary & financial	M1B	YoY %	16.2	12.8	4.1	3.1	3.0	3.1	3.6	4.5	5.4	4.9	5.0	5.2	5.2	4.1	4.1			
	M2	YoY %	8.5	8.0	7.1	5.3	5.3	5.3	5.4	5.6	6.2	6.1	6.0	6.3	6.2	5.8	5.6			
	Foreign reserves	US\$bn	529.9	548.4	554.9	570.6	567.5	570.6	569.5	569.4	568.1	567.0	572.8	573.3	571.7	579.1	577.9	576.9		
	Rediscount rate	%	1.1	1.1	1.8	1.9	1.9	1.9	1.9	1.9	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0		
	Exchange rate	USD/TWD	28.3	27.7	30.7	30.7	31.3	30.7	31.3	31.6	32.0	32.6	32.4	32.4	32.8	32.0	31.7	32.0		

Source: Bloomberg; KGI Research

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