



US FOMC

FFR guessing-game as QE Taper ends

§ Fed announced the completion of QE Taper.

§ Maintain FFR at 0.00%-0.25% and rolling over of purchased assets.

§ Uncertain timing and magnitude of FFR hike amid significant divergence between official guidance and market expectations. We expect 50-75bps hike next year, beginning Sep 2015.

The end of QE Taper. The FOMC meeting on 28-29 Oct 2014 ended with the US Federal Reserve concluding the "QE Taper" i.e. stop the monthly purchases of the agency mortgage-backed securities and the longer-term Treasury securities. To recap, under QE3, Fed purchased USD85b monthly and has gradually cut the monthly purchases since Dec 2013, dubbed "QE Taper".

Fed's balance sheet to stop expanding but stable between now and end-2015. Fed maintains its current policy of reinvesting the principal payments from the agency debt and agency mortgage-backed securities holdings as well as rolling over Treasury securities in its balance sheet to keep long-term interest rate low and the overall financing conditions accommodative. In Sep 2014 FOMC, Fed issued a statement on "policy normalization principles and plan" to communicate with markets on the Fed's monetary policy post-QE Taper. Key takeaways include gradual reduction in Fed's securities holdings in its balance sheet by ceasing or commencing the phasing out reinvestments after increases in the federal funds rate (FFR). Currently, only USD8.8b of purchased assets - or 0.2% of the Fed's total balance sheet size of USD4.4tr - are maturing in the next one year. The longer it takes for Fed to actually raise FFR, the later will the reduction of Fed's balance sheet take place. The Fed balance sheet, while stop expanding, is expected to be stable rather than shrinking in 2015.

Guessing game on the next turning point in Fed's "data dependent" monetary policy. FFR remains at 0%-0.25%, and FOMC statement keeps the reference on maintaining FFR at current level for a considerable time following the end of QE Taper. The accompanying FOMC statement indicated gradually diminishing underutilization of labour resources and receding likelihood of inflation persistently running below 2%, mainly to justify the decision to proceed with ending QE. However, it also points that Fed's next move on monetary policy is "data-dependent". This in view of the remarks that FFR may be hiked sooner or later than currently anticipated depending on whether incoming information on employment and inflation is progressing faster or slower than Fed's expectations.

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Divergence in Fed fund rate (FFR) outlook. Underscoring the guessing game on the timing and magnitude of FFR hike next year is the significant divergence between Fed's guidance, consensus forecast and forward rate.

Fed guidance on FFR implies 125bps hike starting mid-2015. Based on the information from the Sep 2014 FOMC meeting, the majority of Fed's policymakers i.e. (14 out of 17) expects FFR to start increasing in 2015. The Fed officials also raised their median estimate for FFR at the end of 2015 to 1.375% versus 1.125% back in June 2014. On average, this translates into a 125bps hike in FFR next year from the present 0%-0.25%. Assuming a series of consecutive 25bps hikes, and given that there are eight FOMC meetings scheduled for 2015, FFR hikes could begin on the 16-17 June 2015 FOMC meeting.

Consensus forecasts less aggressive. Based on Bloomberg survey of Wall Street economists, FFR is seen rising by a total of 75bps to 1.00% next year. Again, assuming a series of 25bps hikes, consensus is looking at FFR to start rising from the 16-17 Sep 2015 FOMC.

The market-implied forward rate on FFR are even more sanguine about the timing and magnitude of US interest rate hike as it prices in FFR at around 0.50% by end-2015, suggesting FOMC will not make a move on its benchmark interest rate until its very last meeting of next year i.e. 15-16 Dec.

We are siding with markets expectations. Notwithstanding its guidance, Fed is likely to wait for evidence that US growth is truly sustainable and entrenched. At the surface, this is already indicated by the index of leading economic indicators. However, there are uncertainties in outlook of other major economies, especially Eurozone, Japan and China that can have knock on effect to the US economy, on top of the return of global financial market volatility. At the same time, inflation outlook remains benign, thanks to the commodity price situation and prospect. So we are betting that the Fed will err on the side of caution and takes its time to assess all the factors affecting the US economy. We are pricing in 50-75 basis point hikes in FFR beginning Sep 2015.

Note: The dates of FOMC meetings in 2015 are 27-28 Jan, 17-18 Mar, 28-29 Apr, 16-17 June, 28-29 July, 16-17 Sep, 27-28 Oct, 15-16 Dec.

QE Taper (USDb)

FOMC Meetings	Total Monthly Asset Purchase	Chg	Agency Mortgage-Backed Securities	Chg	Longer Term Treasury Securities	Chg
17-18 Dec 2013	75	(10)	35	(5)	40	(5)
28-29 Jan 2014	65	(10)	30	(5)	35	(5)
18-19 Mar 2014	55	(10)	25	(5)	30	(5)
29-30 Apr 2014	45	(10)	20	(5)	25	(5)
17-18 June 2014	35	(10)	15	(5)	20	(5)
29-30 July 2014	25	(10)	10	(5)	15	(5)
16-17 Sep 2014	15	(10)	5	(5)	10	(5)
28-29 Oct 2014	0	(15)	0	(5)	0	(10)

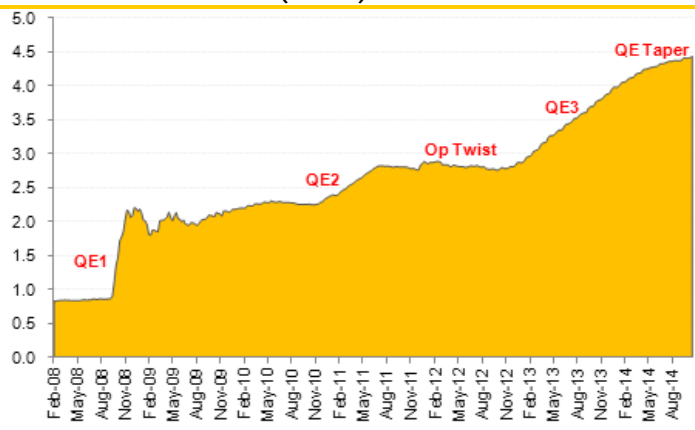
Sources: US Federal Reserve, Maybank KE

Key Timelines of US Quantitative Easing (QE) Policy

Event	Details
QE1 (Dec 2008 - Mar 2010)	<p>On November 25, 2008, Fed announced purchases of up to USD600b in agency mortgage-backed securities (MBS) and agency debt.</p> <p>On December 16, the programme was formally launched by the FOMC.</p> <p>On March 18, 2009, the FOMC announced that the program would be expanded by an additional USD750b in purchases of agency MBS and agency debt and USD300b in purchases of US Treasury securities</p>
QE2 (Nov 2010 - June 2011)	<p>On November 3, 2010, the Fed announced that it would purchase USD600b of longer dated US Treasuries, at a rate of USD75b per month.</p>
Operation Twist (Sep 2011 - Dec 2012)	<p>FOMC announced at its 21 Sep 2011 meeting the implementation of Operation Twist i.e. the purchase of USD400b of bonds with maturities of 6 to 30 years by selling bonds with maturities less than 3 years, thereby extending the average maturity of the Fed's portfolio.</p> <p>Further on 20 June 2012, FOMC announced an extension to Operation Twist by purchasing an additional USD267b of longer-maturity bonds, thereby extending OP Twist throughout 2012.</p>
QE3 (Sep 2012 - Nov 2013)	<p>On September 13, 2012, the Federal Reserve announced QE3 which provided an "open-ended" commitment to purchase USD40b agency mortgage-backed securities per month until the labor market improves "substantially".</p> <p>FOMC meeting on 12 Dec 2012 voted to expand QE3 by adding the purchase of USD45b longer-term US Treasury securities per month, raising the total asset purchase programme to USD85b per month.</p>
QE Taper (Dec 2013 - Oct 2014)	<p>FOMC meeting on 17-18 Dec 2013 announced the reduction in the pace of the Federal Reserve asset purchase programme by USD10b i.e. cutting its monthly purchases of the agency mortgage-backed securities to USD35b from USD40b and the longer-term Treasury securities to USD40b from USD45b. Since then, the Fed has cut its asset purchase programme in the following seven FOMC meetings of 2014 i.e. 28-29 Jan, 18-19 Mar, 29-30 Apr, 18-19 June, 29-30 July, 16-17 Sep & 28-29 Oct.</p>

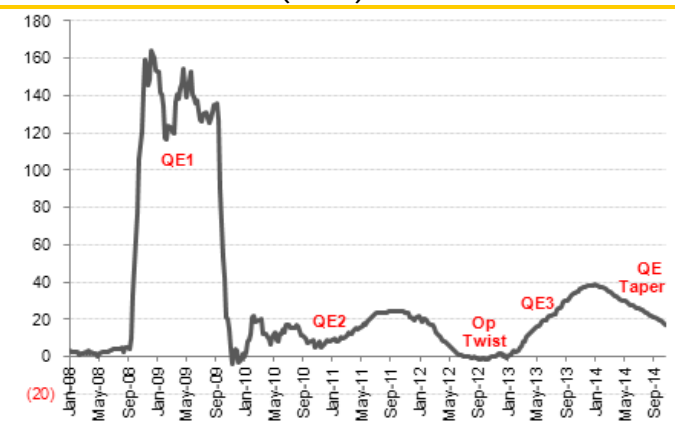
Source: US Federal Reserve

US Fed's Balance Sheet (USD tr)



Source: Bloomberg

US Fed's Balance Sheet (% YoY)



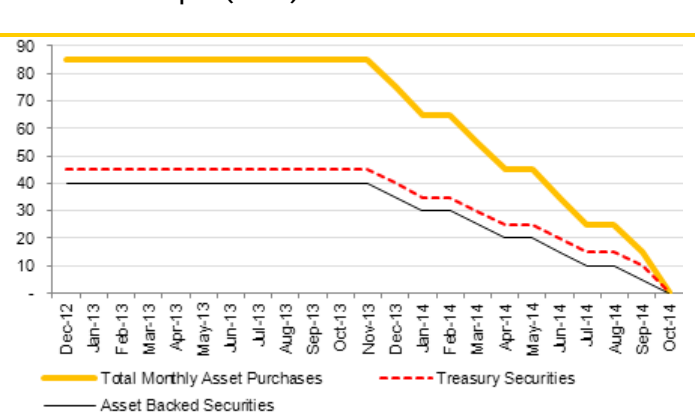
Source: Bloomberg

US Fed's Holdings of Securities in its Balance Sheets, By Types and Maturity (USD\$b, as at 22 Oct 2014)

Maturity Profile	Treasury Securities	Agency Mortgage-Backed Securities	Federal Debts	Total by Securities Maturity	% Share of Total (by Maturity)
15 Days to 90 Days	0.1	0.0	2.1	2.2	0.1
91 Days to 1 Year	3.2	0.0	3.4	6.6	0.2
Over 1 Year to 5 Years	1,050.0	0.0	31.8	1,081.8	25.7
Over 5 Years to 10 Years	743.0	5.2	0.0	748.2	17.8
Over 10 Years	662.9	1,710.2	2.3	2,375.5	56.4
Total by Securities Types	2,459.2	1,715.4	39.7	4,214.3	100.0
% Share of Total (by Asset Types)	58.4	40.7	0.9		

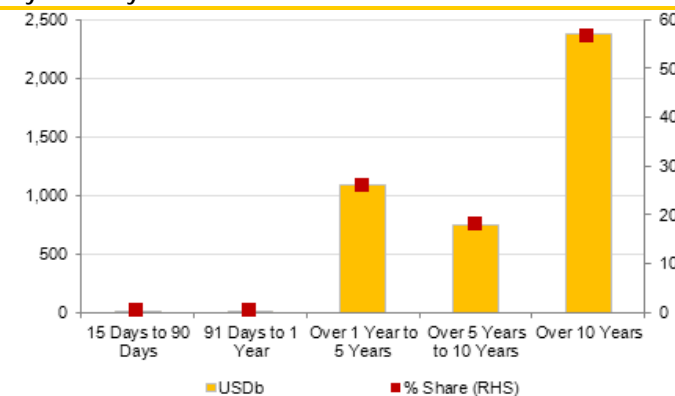
Source: Bloomberg

US Fed's QE Taper (USD\$b)



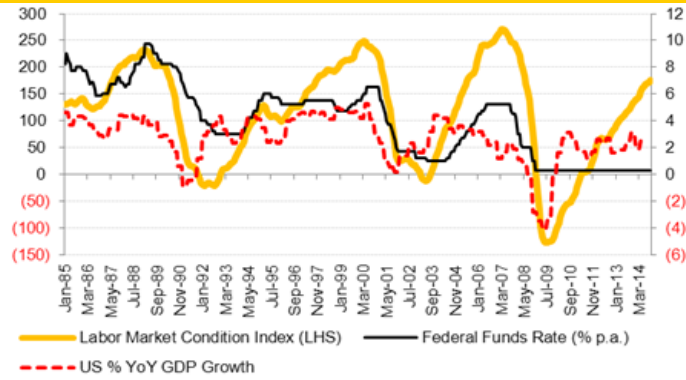
Source: Bloomberg

US Fed's Balance Sheet: Holdings of Purchased Securities by Maturity



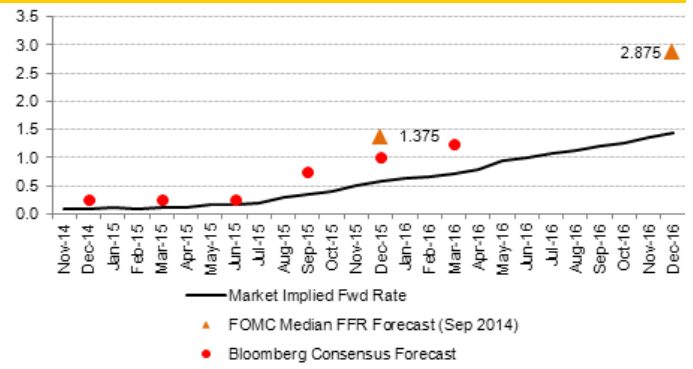
Sources: Bloomberg, Maybank KE

US: Fed Funds Rate, Labour Market Conditions Index, real GDP Growth



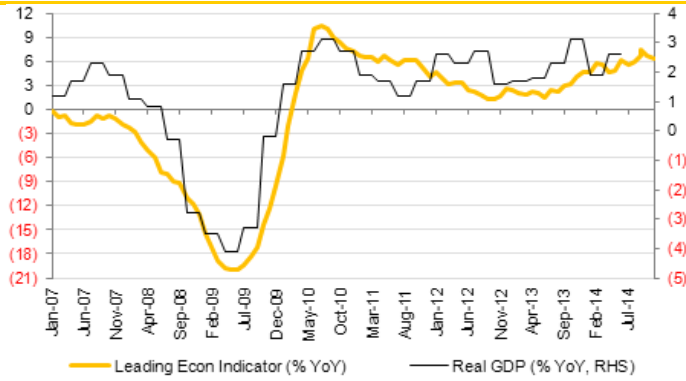
Source: Bloomberg

US Fed Funds Rate: FOMC Guidance, Consensus Forecast & Market Implied Forward Rate



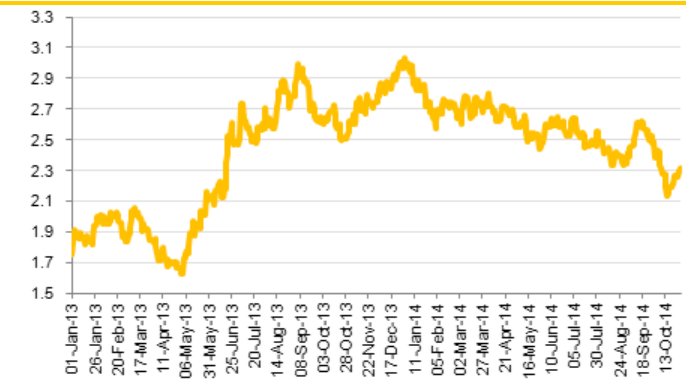
Sources: Bloomberg, US Federal Reserve

US: Real GDP Growth vs Index of Leading Economic Indicators (% YoY)



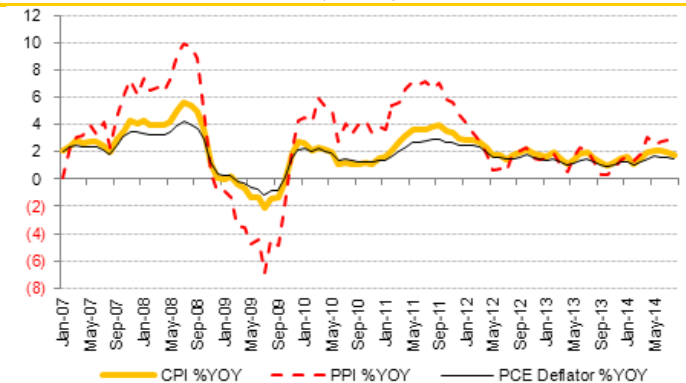
Source: Bloomberg

US: 10-Year Treasury Yields (% p.a.)



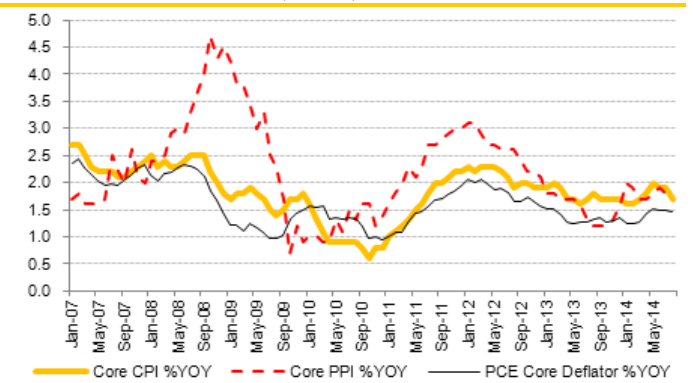
Source: Bloomberg

US: Headline Inflation Rate (% YoY)



Source: Bloomberg

US: Core Inflation Rate (% YoY)



Source: Bloomberg

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