



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.

Economists

Suhaimi Ilias
suhaimi_iliass@maybank-ib.com
(603) 2297 8682

Dr. Zamros Dzulkafli
zamros.d@maybank-ib.com
(603) 2082 6818

Ramesh Lankanathan
ramesh@maybank-ib.com
(603) 2297 8685

William Poh
william.poh@maybank-ib.com
(603) 2297 8683

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)

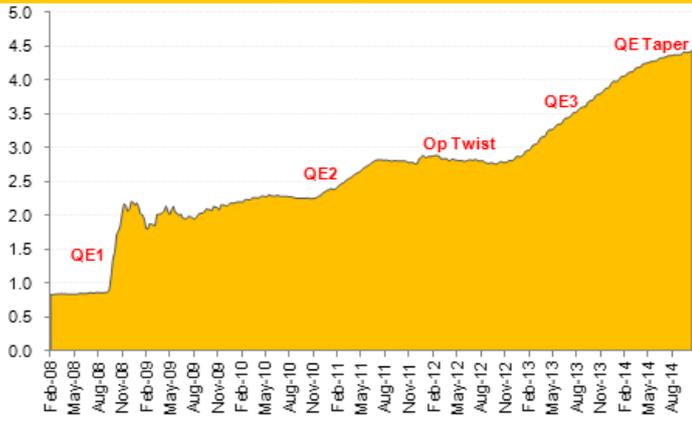
Sources: US Federal Reserve, Maybank KE

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>

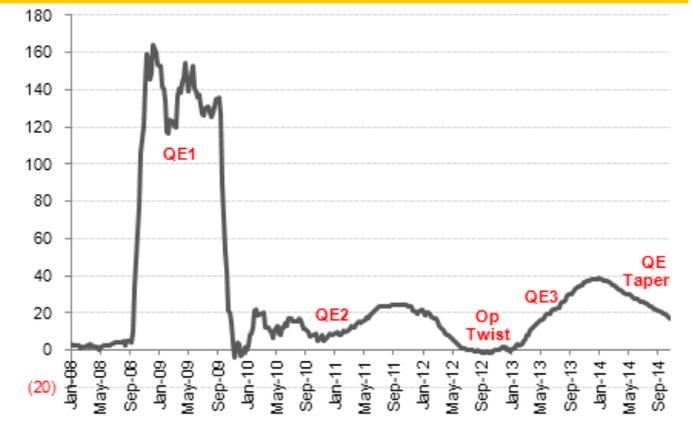
Source: US Federal Reserve

US Fed's Balance Sheet (USD tr)



Source: Bloomberg

US Fed's Balance Sheet (% YoY)



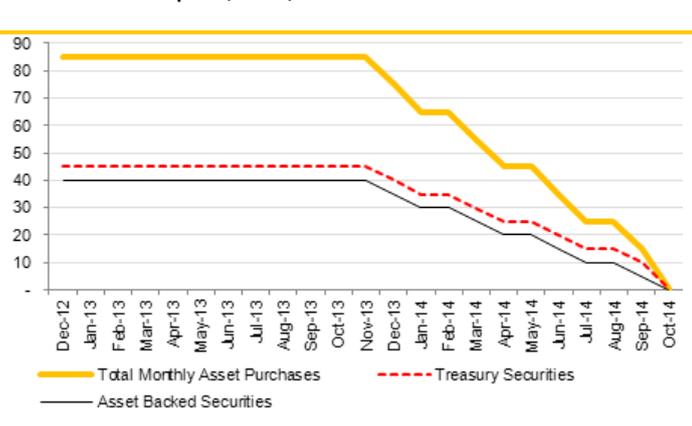
Source: Bloomberg

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		

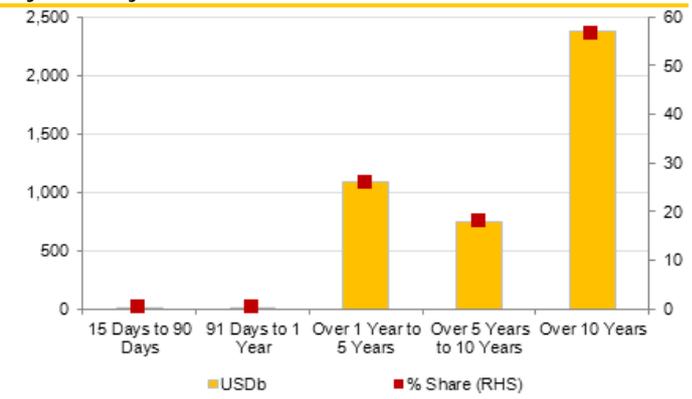
Source: Bloomberg

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



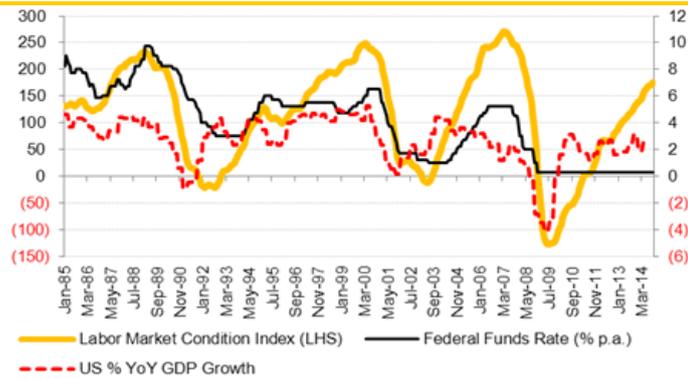
Source: Bloomberg

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



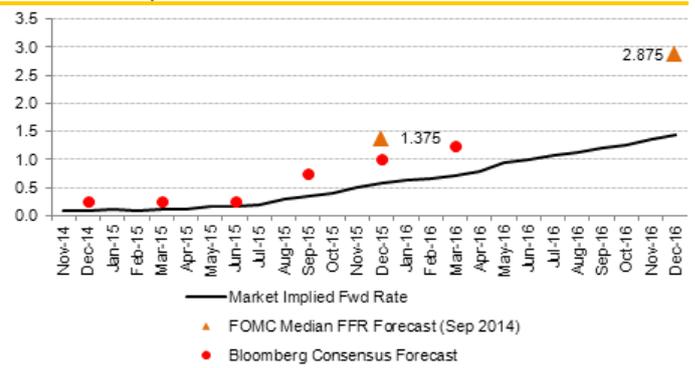
Sources: Bloomberg, Maybank KE

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



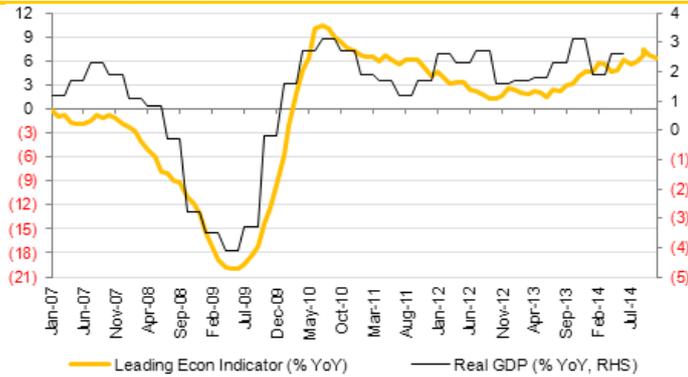
Source: Bloomberg

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)



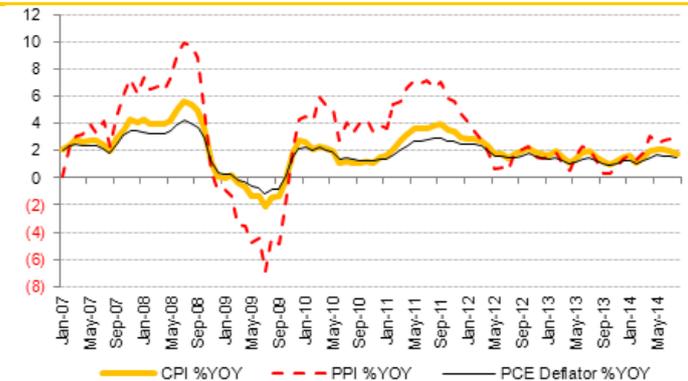
Source: Bloomberg

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



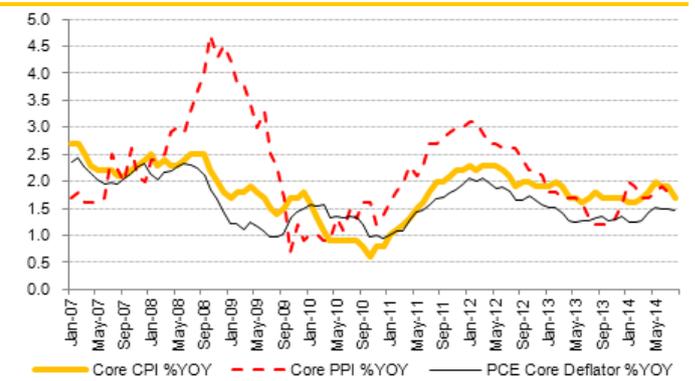
Source: Bloomberg

US: Headline Inflation Rate (% YoY)



Source: Bloomberg

US: Core Inflation Rate (% YoY)



Source: Bloomberg

Research Offices

REGIONAL

WONG Chew Hann, CA
Regional Head of Institutional Research
(603) 2297 8686 wchewh@maybank-ib.com

ONG Seng Yeow
Regional Head of Retail Research
(65) 6432 1453
ongsengyeow@maybank-ke.com.sg

Alexander GARTHOFF
Institutional Product Manager
(852) 2268 0638
alexgarthoff@kimeng.com.hk

ECONOMICS

Suhaimi ILIAS
Chief Economist
Singapore | Malaysia
(603) 2297 8682
suhaimi_ilias@maybank-ib.com

Luz LORENZO
Philippines
(62) 2 849 8836
luz_lorenzo@maybank-atrke.com

Tim LEELAHAPHAN
Thailand
(662) 658 1420 tim.l@maybank-ke.co.th

JUNIMAN
Chief Economist, BII
Indonesia
(62) 21 29228888 ext 29682
Juniman@bankbii.com

MALAYSIA

WONG Chew Hann, CA *Head of Research*
(603) 2297 8686 wchewh@maybank-ib.com
• Strategy • Construction & Infrastructure

Desmond CH'NG, ACA
(603) 2297 8680
desmond.chng@maybank-ib.com
• Banking & Finance

LIAW Thong Jung
(603) 2297 8688 tjliaw@maybank-ib.com
• Oil & Gas - Regional • Shipping

ONG Chee Ting, CA
(603) 2297 8678 ct.ong@maybank-ib.com
• Plantations - Regional

Mohshin AZIZ
(603) 2297 8692 mohshin.aziz@maybank-ib.com
• Aviation - Regional • Petrochem

YIN Shao Yang, CPA
(603) 2297 8916 samuel.y@maybank-ib.com
• Gaming - Regional • Media

TAN Chi Wei, CFA
(603) 2297 8690 chiwei.t@maybank-ib.com
• Power • Telcos

WONG Wei Sum, CFA
(603) 2297 8679 weisum@maybank-ib.com
• Property & REITs

LEE Yen Ling
(603) 2297 8691 lee.yl@maybank-ib.com
• Building Materials • Glove Producers

CHAI Li Shin
(603) 2297 8684 lishin.c@maybank-ib.com
• Plantation • Construction & Infrastructure

Ivan YAP
(603) 2297 8612 ivan.yap@maybank-ib.com
• Automotive

LEE Cheng Hooi *Regional Chartist*
(603) 2297 8694
chenghooi.lee@maybank-ib.com

Tee Sze Chiah *Head of Retail Research*
(603) 2297 6858 szechiah.t@maybank-ib.com

HONG KONG / CHINA

Howard WONG *Head of Research*
(852) 2268 0648
howardwong@kimeng.com.hk
• Oil & Gas - Regional

Alexander LATZER
(852) 2268 0647
alexanderlatzer@kimeng.com.hk
• Metals & Mining - Regional

Jacqueline KO, CFA
(852) 2268 0633 jacquelineko@kimeng.com.hk
• Consumer

Ka Leong LO, CFA
(852) 2268 0630 klo@kimeng.com.hk
• Consumer Discretionary & Auto

Karen KWAN
(852) 2268 0640 karenkwon@kimeng.com.hk
• Property & REITs

Osbert TANG, CFA
(86) 21 5096 8370
osberttang@kimeng.com.hk
• Transport & Industrials

Ricky WK NG, CFA
(852) 2268 0689 rickyng@kimeng.com.hk
• Utilities & Renewable Energy

Steven ST CHAN
(852) 2268 0645 stevenchan@kimeng.com.hk
• Banking & Financials

Warren Lau
(852) 2268 0644
warrenlau@kimeng.com.hk
• Technology - Regional

William YANG
(852) 2268 0675
williamyang@kimeng.com.hk
• Technology - Regional

INDIA

Jigar SHAH *Head of Research*
(91) 22 6632 2632
jigar@maybank-ke.co.in
• Oil & Gas • Automobile • Cement

Anubhav GUPTA
(91) 22 6623 2605
anubhav@maybank-ke.co.in
• Metal & Mining • Capital Goods • Property

Urmil SHAH
(91) 22 6623 2606 urmil@maybank-ke.co.in
• Technology • Media

SINGAPORE

NG Wee Siang *Head of Research*
(65) 6231 5838 ngweesiang@maybank-ke.com.sg
• Banking & Finance

Gregory YAP
(65) 6231 5848 gyap@maybank-ke.com.sg
• SMID Caps - Regional
• Technology & Manufacturing • Telcos

YEAK Chee Keong, CFA
(65) 6231 5842
yeakcheekeong@maybank-ke.com.sg
• Offshore & Marine

Derrick HENG
(65) 6231 5843 derrickheng@maybank-ke.com.sg
• Transport (Land, Shipping & Aviation)

WEI Bin
(65) 6231 5844 weibin@maybank-ke.com.sg
• Commodity • Logistics • S-chips

John CHEONG
(65) 6231 5845 johncheong@maybank-ke.com.sg
• Small & Mid Caps • Healthcare

TRUONG Thanh Hang
(65) 6231 5847 hang.truong@maybank-ke.com.sg
• Small & Mid Caps

INDONESIA

Willianto IE *Head of Research*
(62) 21 2557 1125
willianto.ie@maybank-ke.co.id
• Strategy

Rahmi MARINA
(62) 21 2557 1128
rahmi.marina@maybank-ke.co.id
• Banking & Finance

Aurellia SETIABUDI
(62) 21 2953 0785
aurellia.setiabudi@maybank-ke.co.id
• Property

Isnaputra ISKANDAR
(62) 21 2557 1129
isnaputra.iskandar@maybank-ke.co.id
• Metals & Mining • Cement

Pandu ANUGRAH
(62) 21 2557 1137
pandu.anugrah@maybank-ke.co.id
• Infrastructure • Construction • Transport

Janni ASMAN
(62) 21 2953 0784
janni.asman@maybank-ke.co.id
• Cigarette • Healthcare • Retail

PHILIPPINES

Luz LORENZO *Head of Research*
(63) 2 849 8836
luz_lorenzo@maybank-atrke.com
• Strategy
• Utilities • Conglomerates • Telcos

Lovell SARREAL
(63) 2 849 8841
lovell_sarreal@maybank-atrke.com
• Consumer • Media • Cement

Rommel RODRIGO
(63) 2 849 8839
rommel_rodrigo@maybank-atrke.com
• Conglomerates • Property • Gaming
• Ports/ Logistics

Katherine TAN
(63) 2 849 8843
kat_tan@maybank-atrke.com
• Banks • Construction

Ramon ADVIENTO
(63) 2 849 8845
ramon_adviento@maybank-atrke.com
• Mining

THAILAND

Maria LAPIZ *Head of Institutional Research*
Dir (66) 2257 0250 | (66) 2658 6300 ext 1399
Maria.L@maybank-ke.co.th
• Consumer / Materials

Jesada TECHAHUSDIN, CFA
(66) 2658 6300 ext 1394
Jesada.T@maybank-ke.co.th
• Financial Services

Kittisorn PRUITIPAT, CFA, FRM
(66) 2658 6300 ext 1395
Kittisorn.P@maybank-ke.co.th
• Real Estate

Sittichai DUANGRATTANACHAYA
(66) 2658 6300 ext 1393
Sittichai.D@maybank-ke.co.th
• Services Sector

Sukit UDOMSIRIKUL *Head of Retail Research*
(66) 2658 6300 ext 5090
Sukit.u@maybank-ke.co.th

Mayuree CHOWVIKARAN
(66) 2658 6300 ext 1440
mayuree.c@maybank-ke.co.th
• Strategy

Padon VANNARAT
(66) 2658 6300 ext 1450
Padon.v@maybank-ke.co.th
• Strategy

Surachai PRAMUALCHARONKIT
(66) 2658 6300 ext 1470
Surachai.p@maybank-ke.co.th
• Auto • Conmat • Contractor • Steel

Suttatip PEERASUB
(66) 2658 6300 ext 1430
suttatip.p@maybank-ke.co.th
• Media • Commerce

Sutthichai KUMWORACHAI
(66) 2658 6300 ext 1400
sutthichai.k@maybank-ke.co.th
• Energy • Petrochem

Termporn TANTIVIVAT
(66) 2658 6300 ext 1520
termporn.t@maybank-ke.co.th
• Property

Woraphon WIROONSRI
(66) 2658 6300 ext 1560
woraphon.w@maybank-ke.co.th
• Banking & Finance

Jaroonpan WATTANAWONG
(66) 2658 6300 ext 1404
jaroonpan.w@maybank-ke.co.th
• Transportation • Small cap

Chatchai JINDARAT
(66) 2658 6300 ext 1401
chatchai.j@maybank-ke.co.th
• Electronics

VIETNAM

LE Hong Lien, ACCA
Head of Institutional Research
(84) 844 55 58 88 x 8181
lien.le@maybank-kimeng.com.vn
• Strategy • Consumer • Diversified • Utilities

THAI Quang Trung, CFA, Deputy Manager,
Institutional Research
(84) 844 55 58 88 x 8180
trung.thai@maybank-kimeng.com.vn
• Real Estate • Construction • Materials

Le Nguyen Nhat Chuyen
(84) 844 55 58 88 x 8082
chuyen.le@maybank-kimeng.com.vn
• Oil & Gas

NGUYEN Thi Ngan Tuyen, *Head of Retail Research*
(84) 8 44 555 888 x 8081
tuyen.nguyen@maybank-kimeng.com.vn
• Food & Beverage • Oil&Gas • Banking

TRINH Thi Ngoc Diep
(84) 4 44 555 888 x 8208
diep.trinh@maybank-kimeng.com.vn
• Technology • Utilities • Construction

TRUONG Quang Binh
(84) 4 44 555 888 x 8087
binh.truong@maybank-kimeng.com.vn
• Rubber plantation • Tyres and Tubes • Oil&Gas

PHAM Nhat Bich
(84) 8 44 555 888 x 8083
bich.pham@maybank-kimeng.com.vn
• Consumer • Manufacturing • Fishery

NGUYEN Thi Sony Tra Mi
(84) 8 44 555 888 x 8084
mi.nguyen@maybank-kimeng.com.vn
• Port operation • Pharmaceutical
• Food & Beverage

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Malaysia

Maybank Investment Bank Berhad
(A Participating Organisation of
Bursa Malaysia Securities Berhad)
33rd Floor, Menara Maybank,
100 Jalan Tun Perak,
50050 Kuala Lumpur
Tel: (603) 2059 1888;
Fax: (603) 2078 4194

Stockbroking Business:
Level 8, Tower C, Dataran Maybank,
No. 1, Jalan Maarof
59000 Kuala Lumpur
Tel: (603) 2297 8888
Fax: (603) 2282 5136

Philippines

Maybank ATR Kim Eng Securities Inc.
17/F, Tower One & Exchange Plaza
Ayala Triangle, Ayala Avenue
Makati City, Philippines 1200

Tel: (63) 2 849 8888
Fax: (63) 2 848 5738

South Asia Sales Trading

Kevin Foy
Regional Head Sales Trading
kevinfoy@maybank-ke.com.sg
Tel: (65) 6336-5157
US Toll Free: 1-866-406-7447

Malaysia

Rommel Jacob
rommeljacob@maybank-ib.com
Tel: (603) 2717 5152

Indonesia

Harianto Liong
harianto.liong@maybank-ke.co.id
Tel: (62) 21 2557 1177

New York

Andrew Dacey
adacey@maybank-keusa.com
Tel: (212) 688 2956

Vietnam

Tien Nguyen
thuytien.nguyen@maybank-kimeng.com.vn
Tel: (84) 44 555 888 x8079

Singapore

Maybank Kim Eng Securities Pte Ltd
Maybank Kim Eng Research Pte Ltd
50 North Canal Road
Singapore 059304

Tel: (65) 6336 9090

Hong Kong

Kim Eng Securities (HK) Ltd
Level 30,
Three Pacific Place,
1 Queen's Road East,
Hong Kong

Tel: (852) 2268 0800
Fax: (852) 2877 0104

Thailand

Maybank Kim Eng Securities
(Thailand) Public Company Limited
999/9 The Offices at Central World,
20th - 21st Floor,
Rama 1 Road Pathumwan,
Bangkok 10330, Thailand

Tel: (66) 2 658 6817 (sales)
Tel: (66) 2 658 6801 (research)

North Asia Sales Trading

Alex Tsun
alextsun@kimeng.com.hk
Tel: (852) 2268 0228
US Toll Free: 1 877 837 7635

Thailand

Tanasak Krishnasreni
Tanasak.K@maybank-ke.co.th
Tel: (66)2 658 6820

London

Simon Lovekin
simonl@maybank-ke.co.uk
Tel: (44)-207-626-2828

India

Manish Modi
manish@maybank-ke.co.in
Tel: (91)-22-6623-2601

Philippines

Keith Roy
keith_roy@maybank-atrke.com
Tel: (63) 2 848-5288

London

Maybank Kim Eng Securities
(London) Ltd
5th Floor, Aldermay House
10-15 Queen Street
London EC4N 1TX, UK

Tel: (44) 20 7332 0221
Fax: (44) 20 7332 0302

Indonesia

PT Maybank Kim Eng Securities
Plaza Bapindo
Citibank Tower 17th Floor
JI Jend. Sudirman Kav. 54-55
Jakarta 12190, Indonesia

Tel: (62) 21 2557 1188
Fax: (62) 21 2557 1189

Vietnam

Maybank Kim Eng Securities Limited
4A-15+16 Floor Vincom Center Dong
Khoi, 72 Le Thanh Ton St. District 1
Ho Chi Minh City, Vietnam

Tel : (84) 844 555 888
Fax : (84) 8 38 271 030

New York

Maybank Kim Eng Securities USA
Inc
777 Third Avenue, 21st Floor
New York, NY 10017, U.S.A.

Tel: (212) 688 8886
Fax: (212) 688 3500

India

Kim Eng Securities India Pvt Ltd
2nd Floor, The International 16,
Maharishi Karve Road,
Churchgate Station,
Mumbai City - 400 020, India

Tel: (91) 22 6623 2600
Fax: (91) 22 6623 2604

Saudi Arabia

In association with
Anfaal Capital
Villa 47, Tujjar Jeddah
Prince Mohammed bin Abdulaziz
Street P.O. Box 126575
Jeddah 21352

Tel: (966) 2 6068686
Fax: (966) 26068787