

U.S. Federal Funds Rate – A hold?

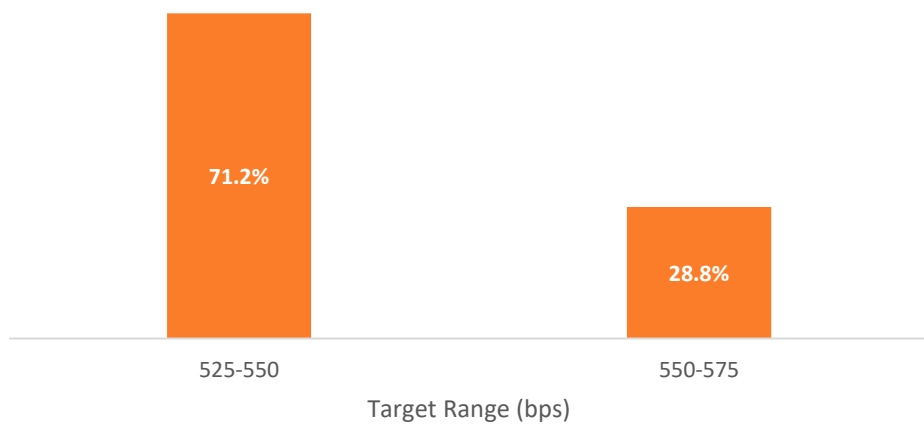
The U.S. FOMC held rates steady on expected lines. The tone of the statement was similar to the one in September – strong economic activity, resilient banking system, tighter credit conditions with an uncertain impact, focus on bringing down inflation, and data dependent future actions. However, while the September policy had strong hints of an additional rate hike in 2023, the November policy did not give any specific signal to this effect. The FOMC has held rates steady in a range of 5.25% to 5.5% since July 2023. U.S. inflation has moderated to 3.4% in September from a peak of 7.1% in June.

While the Fed adjusts short-term rates, it impacts the long-term rates with a lag. The 10-year U.S. Treasury yield (which forms the base for other interest rates in the market) has risen 100bps in less than three months and crossed 5% in October - for the first time since 2007. Fed Chair Powell acknowledged that monetary policy is restrictive, and its effects are visible. Higher rates will lead eventually lead to higher default rates for companies and individuals, weighing down on growth, which could push the economy away from a soft landing. The Fed chair acknowledged that the risks of doing too little to tackle inflation versus doing too much had become more “two-sided”. Inflation cooling off to 2% with rates remaining high would also suggest that the neutral rate has moved higher. This would provide ammunition to the Fed to act when recession hits.

The November statement and press conference by Fed Chair Powell indicates a possibility that the U.S. Fed might be comfortable with a hold for now. It seems the focus has shifted from how high rates should be to how long should the higher rates prevail. The September statement did strongly indicate a 25bps in the remainder of 2023. While the Fed has left all options open to bring down inflation within 2%, the odds of a hike in December 2023 look diminished after yesterday’s statement.

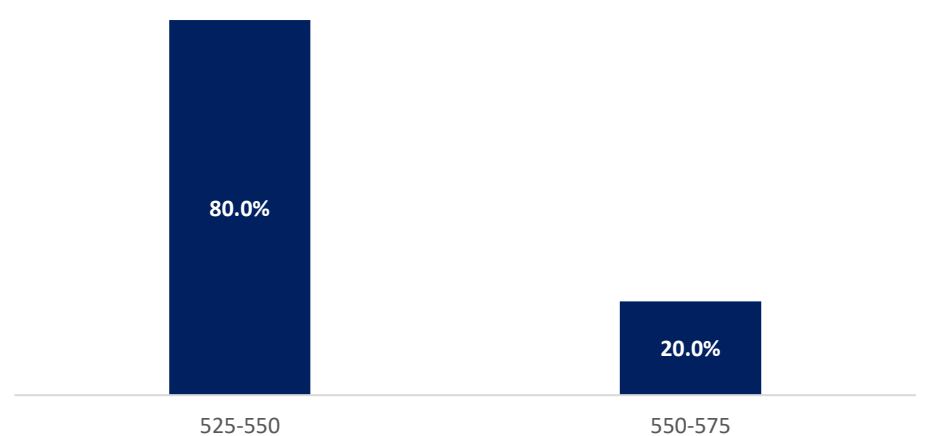
CME Fed Watch Tool

Target rate probabilities for November 1, 2023 meeting



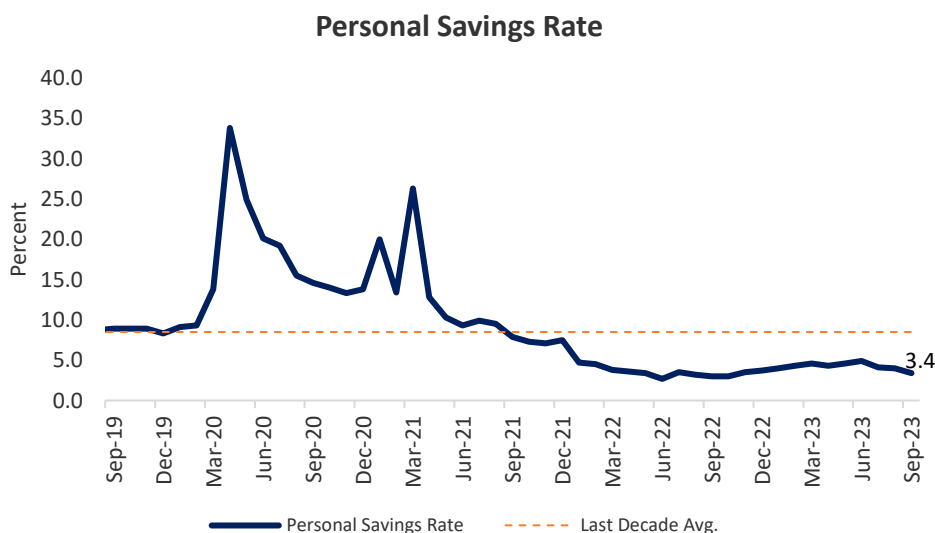
Probabilities as on Oct 31

Target rate probabilities for December 13, 2023 meeting



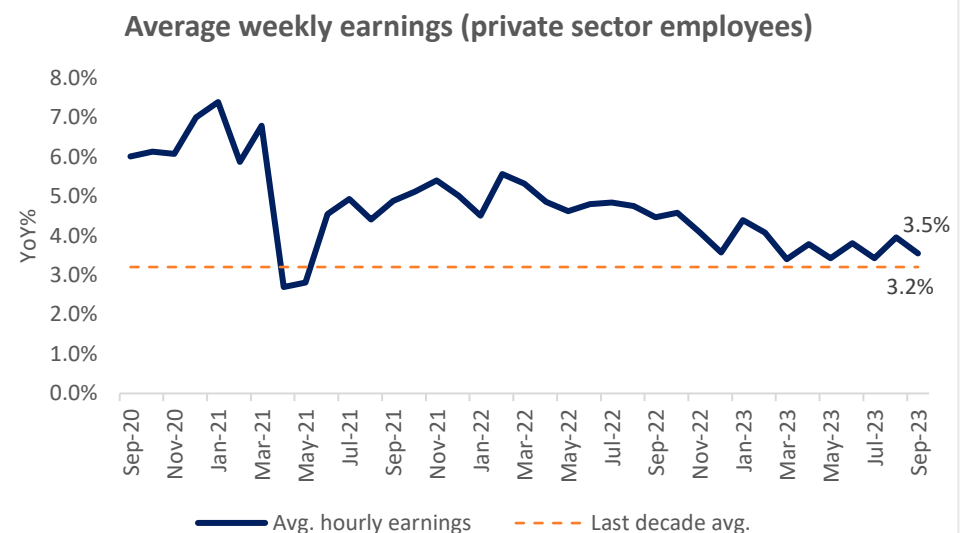
Probabilities as on Nov 2

Personal savings rate declined 21% in FYTD24

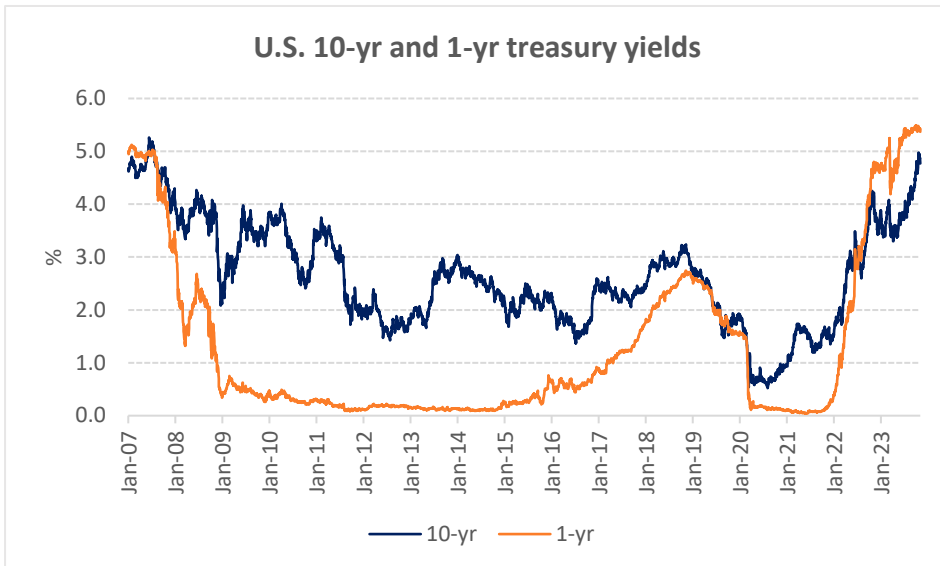


Source: CME Fed, FRED, TruBoard

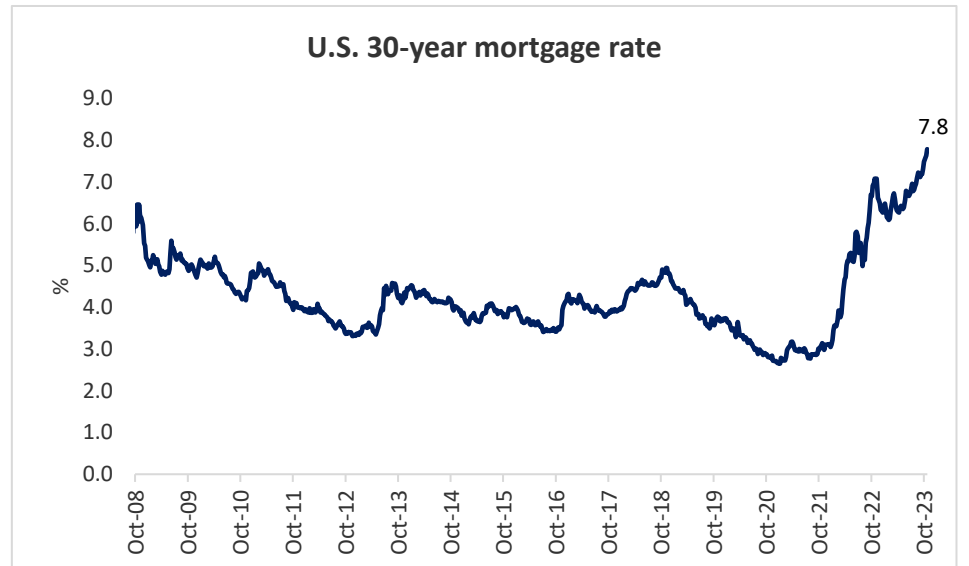
Earnings growth stronger than last decade



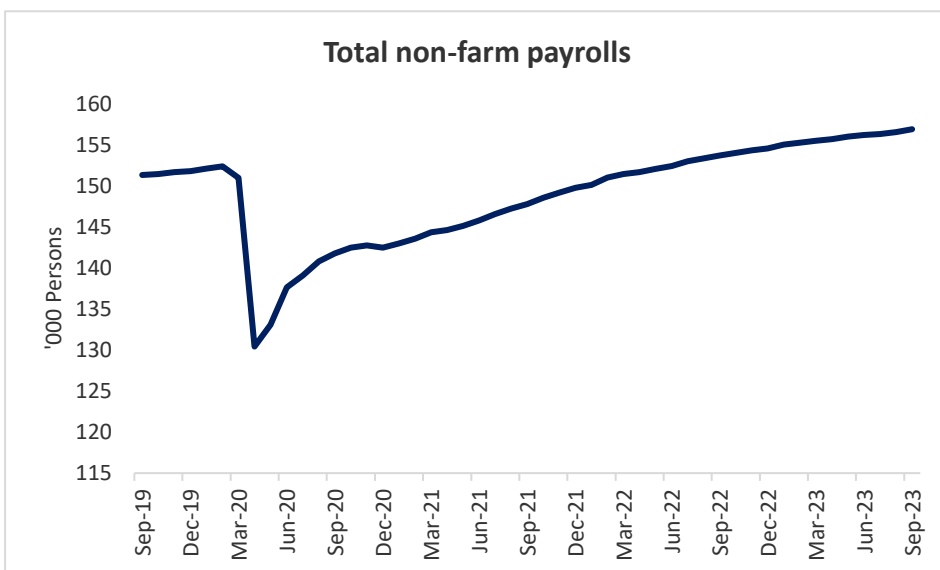
U.S. treasury yields at a 16-year high



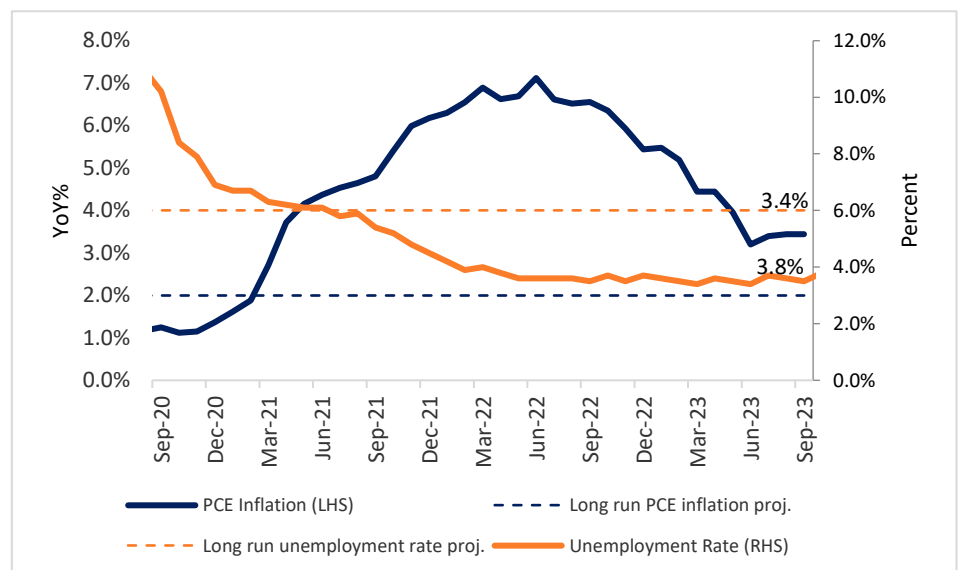
U.S. 30-year mortgage rates plummeting loan applications



Payrolls soared by 3,36,000 in September 2023



Inflation and unemployment beating Fed's target



Positive values indicate tighter than average liquidity conditions, negative values indicate loose financial conditions

Source: FRED, TruBoard

Market Reactions

	Opening date	Opening value	Closing date	Closing value	% Change
Dow Jones Industrial	01-11-2023	33081.87	01-11-2023	33274.58	0.58%
DXY	01-11-2023	106.67	01-11-2023	106.88	0.20%
S&P 500	01-11-2023	4201.27	01-11-2023	4237.86	0.87%
U.S. 10 Year G-sec	01-11-2023	4.92%	01-11-2023	4.77%	-3.05%
	Closing date	Closing value	Opening date	Opening value	% Change
Nikkei 225	01-11-2023	31601.65	02-11-2023	31987.02	1.22%
Sensex	01-11-2023	63591.33	02-11-2023	64040.10	0.71%
INR/USD	01-11-2023	83.28	02-11-2023	83.25	-0.04%
India 10 Year G-Sec	01-11-2023	7.36%	02-11-2023	7.32%	-0.54%
India Call Money Rate (Wtd. Avg.)	01-11-2023	6.77%	02-11-2023	6.78%	0.15%

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