

ASIA PACIFIC



## ECONOMIC UPDATE

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## US FOMC - No tapering yet

*The Fed delivered a positive surprise by keeping the status quo on its QE programme amid broad-based moderate economic improvement, in contrast to market expectations of a tapering announcement. While this move provides some temporary respite for the market, it will lead to prolonged market uncertainty as investors recalibrate expectations towards a tapering announcement during the next two FOMC meetings on 28-29 Oct and 16-17 Dec. Adding to the uncertainty are the upcoming budget and debt-ceiling battles in Oct.*

“ We could begin later this year. But even if we do that, the subsequent steps will be dependent on continued progress in the economy. So we are tied to the data. We don't have a fixed calendar schedule.

–Ben Bernanke, Fed Chairman

### Fed needs more time to decide... »

Contrary to market expectations of a tapering announcement, the Fed has decided to keep its asset-purchase programme unchanged after the conclusion of a two-day meeting. The Fed decided to await more evidence that economic progress will be sustained before adjusting the pace of its purchases. Although this move provides some temporary respite for the market, it will cause prolonged market uncertainty as investors recalibrate expectations towards a tapering announcement during the next two FOMC meetings on 28-29 Oct and 16-17 Dec. Adding to the uncertainty are the upcoming budget and debt-ceiling battles in Oct and the Fed chair selection process.

### ...amid still-decent economic data flows »

The Fed sees continued moderate economic growth amid some improvement in the labour market. Household spending and business fixed investment advanced, while the housing sector has been strengthening. Nevertheless, the Fed downgraded this year's GDP growth estimate to 2.0-2.3% from 2.3-2.6%. Its unemployment rate projection was roughly maintained at 7.1-7.3%. For 2014, the Fed also revised down its GDP growth to 2.9-3.1% (3.0-3.5% previously), while unemployment will be at 6.4-6.8% (6.5-6.8% previously).

### Focus on Fed's forward guidance »

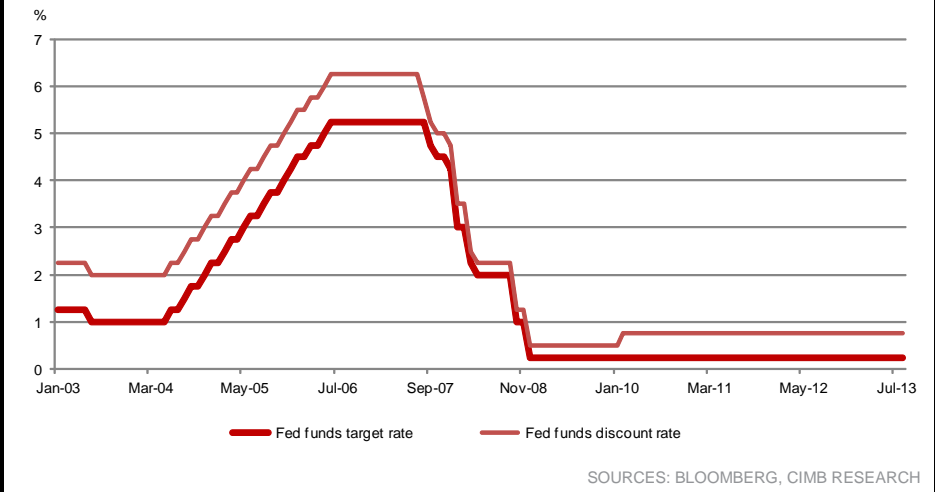
Fed Chairman Ben Bernanke reiterated that the tapering plan was never a "preset course" and indicated that the Fed's plan to taper this year is still on track, contingent on its assessment of the economic outlook. In our view, the Fed's interest-rate normalisation will be a lengthy process that could last well into 2015, beginning with the tapering of the pace of QE3 and going on to ending QE3 (stop purchasing completely), shrinking its balance sheet (either by running off positions or selling) and finally, gradually raising the Fed funds rate. Currently, the Fed has linked its interest-rate normalisation to the unemployment rate (6.5%), a threshold it has conditionally set to begin raising interest rates.

**Figure 1: Economic projections of the Federal Reserve**

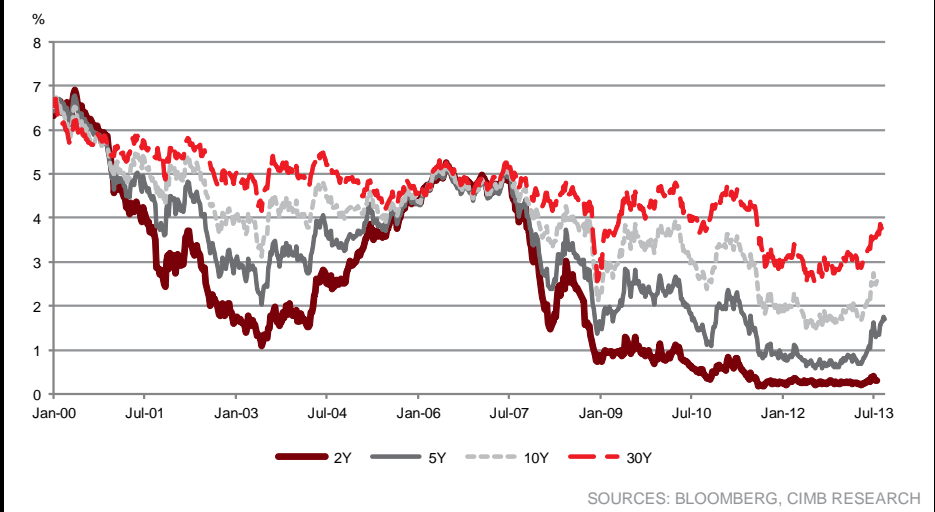
	2013		2014		2015		Longer run	
	New	Old (Jun est.)	New	Old (Jun est.)	New	Old (Jun est.)	New	Old (Jun est.)
Real GDP	2.0 - 2.3	2.3 - 2.6	2.9 - 3.1	3.0 - 3.5	3.0 - 3.5	2.9 - 3.6	2.2 - 2.5	2.3 - 2.5
Unemployment rate	7.1 - 7.3	7.2 - 7.3	6.4 - 6.8	6.5 - 6.8	5.9 - 6.2	5.8 - 6.2	5.2 - 5.8	5.2 - 6.0
PCE inflation	1.1 - 1.2	0.8 - 1.2	1.3 - 1.8	1.4 - 2.0	1.6 - 2.0	1.6 - 2.0	2.0	2.0
Core PCE inflation	1.2 - 1.3	1.2 - 1.3	1.5 - 1.7	1.5 - 1.8	1.7 - 2.0	1.7 - 2.0	-	-

SOURCES: FEDERAL RESERVE, CIMB RESEARCH

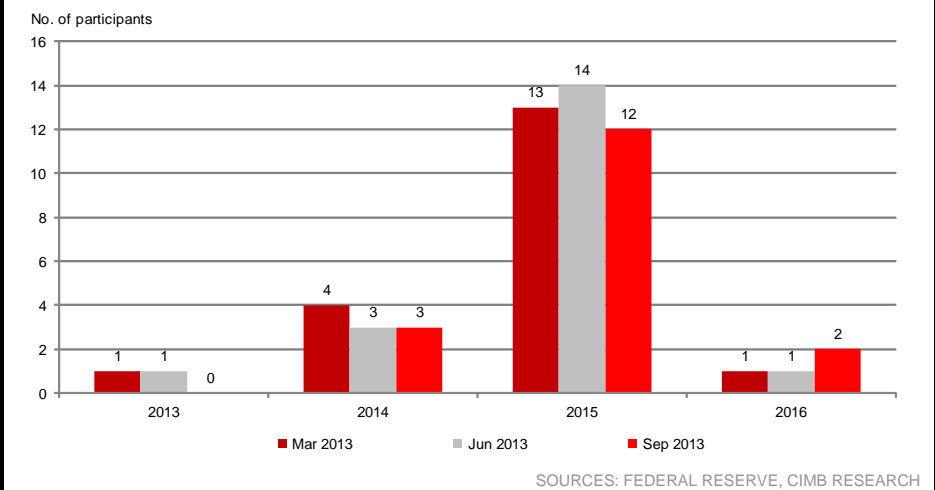
**Figure 2: Fed to keep rate at 0.0-0.25% for the foreseeable future**



**Figure 3: US Treasury yields rising**



**Figure 4: More FOMC participants think the first rate hike to come in 2015**



**Figure 5: Fed responses to financial market events and recessions**

Year(s)	Event	Fed funds target rate	Period	Quantum of rate cuts (bps)	Frequency of rate cuts
1974-75	Recession - Oil crisis coupled with high government spending due to Vietnam war	13.00% to 5.25%	Jul-74  Apr-75	775	12
1980	Recession - Oil crisis triggered by Iranian revolution	20.00% to 9.50%	Mar-80  Jul-80	1,050	3
1981-82	Recession - Tight monetary policy to control high inflation	20.00% to 8.50%	May-81  Dec-82	1,150	12
1987	Stock-market crash on 20 Oct 1987	No target rate from 19 Oct to 3 Nov 1987	-	-	-
1990-91	Recession - Collapse of savings and loans and restrictive monetary policy	8.25% to 3.00%	Jul-90  Dec-92	525	18
1998	Long-Term Capital Management crisis	5.50% to 4.75%	Aug-98  May-99	75	3
2001-03	Recession - Dot Com bubble burst, 11 Sep terrorist attacks, accounting scandals	6.50% to 1.00%	Dec-01  Jun-03	550	13
2007	Subprime crisis fallout - housing recession	5.25% to 4.25%	Sep-07  Dec-07	100	3
2008	Downside risks to growth, financial market stress	4.25% to 0.00% - 0.25%	Jan-08  Oct-08	400-425	7
2009	Economy enters recovery, financial sector recovers but banking sector still weak and unemployment rate exceeds 10%	No change in rates; held at 0.00% - 0.25%	-	-	-
2010-13	Bumps in economic recovery, unemployment rate remains high, housing market still weak	No change in rates; rates to stay at 0.00% - 0.25% for the foreseeable future	-	-	-

SOURCES: FEDERAL RESERVE, CIMB RESEARCH

**Figure 6: The majority of Fed participants still expect the first rate hike to only happen in 2015, unchanged from the Jun meeting**

Target Federal Funds Rate at Year-End (%)	2013	2014	2015	2016	Longer run
	Number of FOMC participants				
0.25	17 (18)	14 (15)	2 (1)		
0.50	- (1)		1 (2)	1 (-)	
0.75			5 (3)		
1.00		2 (3)	3 (4)	1 (-)	
1.25		1 (-)	1 (2)		
1.50		- (1)	2 (3)	1 (-)	
1.75				5 (-)	
2.00			- (1)	2 (-)	
2.25					
2.50				2 (-)	
2.75				2 (-)	
3.00			2 (3)		
3.25			1 (-)		1 (1)
3.50					2 (2)
3.75					1 (1)
4.00				2 (-)	10 (9)
4.25				1 (-)	3 (3)
4.50					- (3)

( ) previous projections in Jun

SOURCES: FEDERAL RESERVE, CIMB RESEARCH

**Figure 7: Historical Fed actions and FOMC scheduled meetings in 2011-2015**

Year	Policy meeting dates	Rate change (bps)	Fed funds rate (%)
2015	27-28 Jan	-	-
2014	16-17 Dec	-	-
	28-29 Oct	-	-
	16-17 Sep	-	-
	29-30 Jul	-	-
	17-18 Jun	-	-
	29-30 Apr	-	-
	18-19 Mar	-	-
	28-29 Jan	-	-
2013	17-18 Dec	-	-
	29-30 Oct	-	-
	17-18 Sep	No change	0.00 - 0.25
	30-31 Jul	No change	0.00 - 0.25
	18-19 Jun	No change	0.00 - 0.25
	30 Apr-1 May	No change	0.00 - 0.25
	19-20 Mar	No change	0.00 - 0.25
2012	29-30 Jan	No change	0.00 - 0.25
	11-12 Dec	No change	0.00 - 0.25
	23-24 Oct	No change	0.00 - 0.25
	12-13 Sep	No change	0.00 - 0.25
	31 Jul-1 Aug	No change	0.00 - 0.25
	19-20 Jun	No change	0.00 - 0.25
	24-25 Apr	No change	0.00 - 0.25
	13-Mar	No change	0.00 - 0.25
2011	24-25 Jan	No change	0.00 - 0.25
	13-Dec	No change	0.00 - 0.25
	1-2 Nov	No change	0.00 - 0.25
	20-21 Sep	No change	0.00 - 0.25
	9-Aug	No change	0.00 - 0.25
	21-22 Jun	No change	0.00 - 0.25
	26-27 Apr	No change	0.00 - 0.25
	15-Mar	No change	0.00 - 0.25
25-26 Jan	No change	0.00 - 0.25	

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