Daiwa Capital Markets

U.S. Economic Comment

- Updated Fed call: on track for neutral amid somewhat fewer cuts
- S&P Flash PMIs: manufacturing sector sluggish, while service sector activity remained firm

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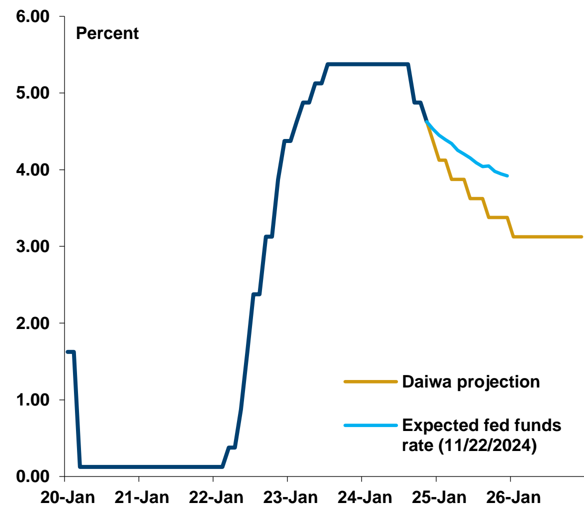
The Path of Policy in Late 2024 & Beyond

Much has changed since September, when we last updated our Fed call. Donald Trump was elected as the 47th President of the United States, with Republicans retaining control of the House of Representatives and gaining the majority in the Senate, all while the economy again registered a strong performance (GDP growth of 2.8 percent, annual rate, in Q3) amid ongoing labor market normalization and inflation remained, in the words of Chair Powell, on a “sometimes bumpy path” back toward the Federal Reserve’s two-percent inflation objective. These developments do not call for a significant reappraisal of our previous call, but they do suggest the need for adjustment at the margin. That is, the reauthorization of pro-growth tax cuts by the incoming administration, along with potentially inflationary trade policy centered on tariffs, raise the possibility of slower cuts by the FOMC (100 basis points of reductions in 2025 versus 150 projected previously, and a higher floor for the federal funds rate -- 3.125 percent by year-end 2026 versus 2.875 percent previously), as does the recent attenuation of prior rapid improvement in underlying inflation. Consequently, we have revised our year-end targets for the federal funds rate for both next year and 2026.

The Projected Trajectory of the Federal Funds Rate

With a recalibration in policy now well underway, including 75 basis points in rate cuts at the past two FOMC meetings, we suspect that policymakers are committed to further easing in the policy rate beyond what is currently implied by pricing in fed funds futures contracts (a spread of approximately 50 basis points as of year-end 2025; chart) – a view crystalized by Chicago Fed President Austan Goolsbee, who indicated in a speech this week that rates by the end of next year ought to be “a fair bit lower than where they are today.” As such, we anticipate that the Committee will reduce the target range for the federal funds rate by 25 basis points at the December to a range of 4-1/4 to 4-1/2 percent (4.375 percent midpoint), despite futures contracts indicating only a 52 percent probability of a cut as of Friday afternoon. Additionally, we look for the FOMC to implement reductions of 25 basis points at the January and March 2025 meetings (target range of 3-3/4 to 4 percent following the March gathering; 3.875 percent midpoint) and then pausing at the May meeting to assess policy objectives. We then expect additional cuts of 25 basis points at the June and September meetings followed by the maintenance of a target range of 3-1/4 to 3-1/2 percent (3.375 percent midpoint) into year-end 2025 (versus 2-3/4 to 3 percent projected previously). Contingent on inflation and labor market conditions evolving favorably, an additional reduction is possible in 2026 (terminal range of 3 to 3-1/4 percent, 3.125 percent midpoint).

Federal Funds Target Rate*



** The gold bar is DCMA’s forecast through year-end 2026 while the light blue bar is based off of futures pricing data through year-end 2025.*

Sources: Federal Reserve Board via Haver Analytics; Daiwa Capital Markets America; Bloomberg

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Heightened Uncertainty

We readily admit that a good bit of uncertainty surrounds our current projection, with a variety of variables prompting a rethink of our Fed call -- possibly as soon as the release of the new Summary of Economic Projections following the December 17-18 FOMC meeting. Specifically, we are perhaps less concerned about near-term implications of Trump's economic policies than those now forecasting a shallower path of rate cuts. Thus, we remain more so attuned to the near-term data.

Regarding the economic policies associated with the incoming Trump administration, we are currently inclined to avoid hyperventilating over potential inflationary effects of proposed tariffs and extensions of tax cuts. Prior rounds of tariffs and renegotiation of various trade pacts did not stir significant price pressure during the previous Trump administration. Additionally, we suspect that current proposals are a negotiating tactic rather than a bona fide policy prescription. The President-elect, who very much views himself as a populist, would likely refrain from policies that disproportionately inflict economic pain on key constituencies. On the tax front, we see extensions of many (all?) provisions of the Tax Cuts and Job Acts as mainly preventing contractionary fiscal policy rather than providing a new tailwind to growth (and possibly inflation). Broadly speaking, until the new Congress actively debates President Trump's proposals and advances legislation, we're sympathetic to Chair Powell's sentiments at his November 7 post-FOMC press conference: "There's nothing to model right now."

Again, more pertinent to the path of policy will be near-term development with respect to inflation and the labor market. With the economy remaining on track into year-end (we expect Q4 growth in the upper-one-percent area) and the labor market appearing to have found a possibly sustainable equilibrium (recent hurricane-related disruptions aside), upside risks to inflation are still very much on the minds of policymakers, particularly as progress on the price front has slowed in recent months and core inflation measured by the price index for personal consumption expenditures is expected to record year-over-year growth of 2.8 percent in October (to be published 11/27). With that in mind, deviations from Fed projections of either inflation or unemployment could draw more resolute action from the FOMC – keeping rates higher for longer in response to sticky inflation, or cutting more rapidly amid weaking in underlying labor market conditions. Time will tell. To reiterate, our current expectations for the economy and inflation point us in the direction of anticipating further more measured cuts at upcoming FOMC meetings before a slowing in the pace of reductions later in 2025. With the risks to achieving their employment and inflation objectives now roughly in balance, it's imperative for officials to take a cautious approach in assessing incoming data and external developments when deciding policy.

Friday Data: S&P Flash PMI Points to Ongoing Economic Expansion

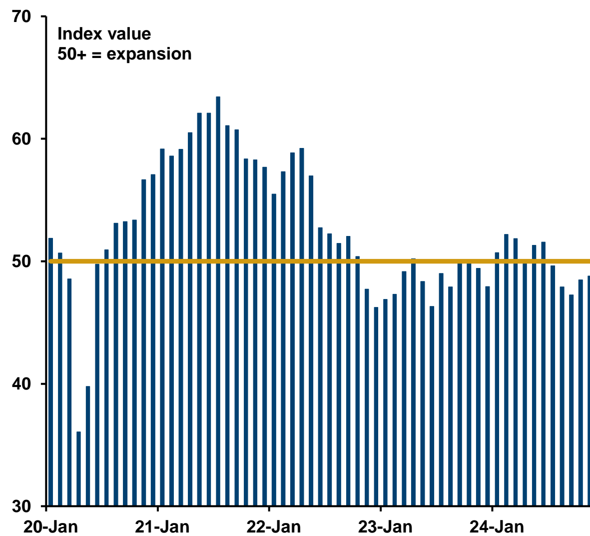
The November flash (preliminary) estimate of the S&P Global composite PMI for the U.S. printed above expectations today (55.3 versus the Bloomberg median projection of 54.3 – a pickup of 1.2 percentage points from the October reading). The latest result contributed to the broad body of evidence that the U.S. economy remains on a growth track, a "soft landing" scenario hopefully sustained by the ongoing recalibration in monetary policy (see previous story). Aligning with the recent performance, the manufacturing sector remained in contraction, constrained by headwinds generated by previously restrictive monetary policy, while the service sector of the economy – which covers a broad array of industries and makes up a significant share of gross value added to economic activity – continued to perform well.

Despite a pickup in in the latest month, the manufacturing PMI suggested that the sector continued to underperform the broader economy. While the index rose 0.3 point to 48.8 (slightly less firm than the Bloomberg consensus expectation of an uptick of 0.4 point to 48.9), it still remained under the critical threshold of 50 which separates expansion from contraction. Moreover, while November's observation was the fifth consecutive contractionary reading, this PMI has posted a sub-50 reading in 19 of the past 25 months (chart, next page, below left). The performance across the subcomponents was decidedly mixed. Notably, the output subindex (also referred to as production) slipped further below 50, dropping 2.9 points to a 23-month low of 46.3. Also, the new orders component, while increasing 1.1 points 47.9, remains mired in contractionary territory. Employment, meanwhile, rose 1.9 points to 50.8, its first reading in expansion territory since last July.

On the prices front, inflationary pressure was subdued. Input prices (what's charged to manufacturers) fell 2.1 points to 52.8, while output prices (what manufacturers charge) rose 0.3 point to 53.5. Even with November's observations indicating higher prices, the shifts were marginal rather than acute – nowhere near levels approached during the peak of the inflationary pout earlier in the expansion (87.6 for input prices in November 2021 and 76.4 in October 2021 for output prices).

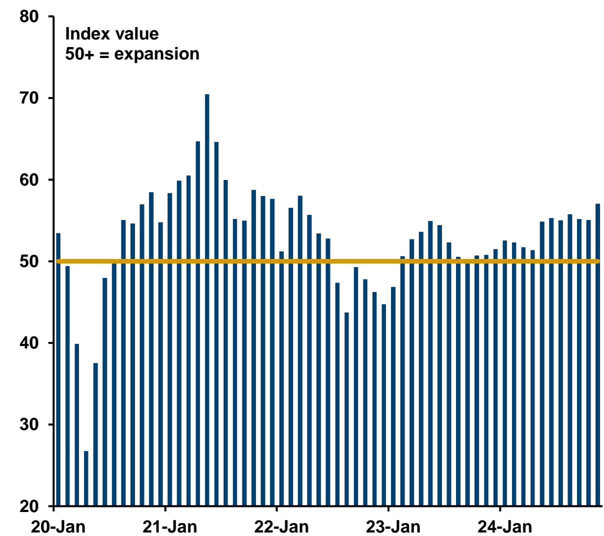
The service sector, on the other hand, stood out as an ongoing engine of growth. Specifically, November's flash estimate for the S&P Global service PMI saw the measure rise 2.0 points to 57.0, beating the market expectation of no change and posting the highest reading since an observation of 58.0 in March 2022 (chart, below right). New export orders, backlogs of work, and new business stood out on the firm side, with the components rising by 3.0, 2.9, and 2.0 points, respectively, to 53.3, 52.9, and 56.1 in the latest month. The employment index, however, eased 0.9 point to 48.7, its fourth straight reading in contractionary territory. Again, price pressure was lacking in the services sector: both input and output prices fell in November, decreasing 1.4 and 1.5 points, respectively, to 57.4 and 50.3. All told, manufacturing activity has to emerge from the doldrums, but the service sector (and the U.S. economy as a whole) remains on track into year-end 2024.

US PMI: Manufacturing



Source: S&P Global via Haver Analytics

US PMI: Services



Source: S&P Global via Haver Analytics

Note to readers:

The next Weekly Economic Comment will be published on December 6, 2024.

The Week Ahead

New Home Sales (October) (Tuesday)
Forecast: 0.720 Million (-2.4%)

Although there was a modest pickup in buyer traffic in October, an increase in mortgage interest rates and an easing in mortgage applications for a home purchase suggest that new home sales could decline after an increase of 4.1 percent to 0.738 million units, annual rate, in the prior month. That said, while affordability constraints still remain in place, new home sales have outperformed (to a degree) the existing homes portion of the market. Even with some projected cooling, activity could remain in the upper-end of the range of the past two years (comparable to the performance seen prior to the pandemic).

Consumer Confidence (November) (Tuesday)
Forecast: 113.0 (+4.0%)

With the U.S. presidential election now in the rear-view mirror, consumer focus can return to moderating inflation and a still-favorable labor market that's supportive of solid wage growth. These positive fundamentals raise the possibility of a second consecutive gain in confidence, with the potential to register the highest reading since the summer of last year (114.0 in July 2023). With that said, the projected level would still be well below pre-pandemic observations.

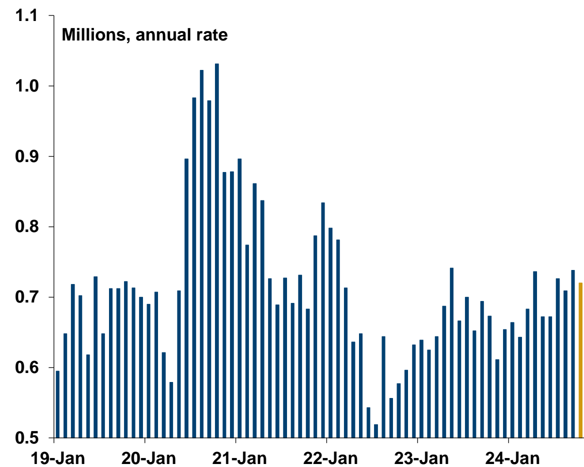
Revised GDP (2024-Q3) (Wednesday)
Forecast: 2.8% (Unrevised)

Data released since the first publication of GDP (October 30) suggest that output in the third quarter was close to the advance tally. In that regard, consumer spending is likely to remain a key driver of growth (+2.46 percentage points to growth in Q3), while net exports could exert a notable drag (-0.56 percentage point to growth).

Durable Goods Orders (October) (Wednesday)
Forecast: +1.0% Total, +0.2% Ex. Transportation

Despite ongoing quality control issues at Boeing, and associated sharp volatility in monthly order flows, bookings increased in October and thus could contribute to an advance in total durable orders. Bookings excluding transportation have tilted slightly higher in 2024 despite ongoing headwinds in the factory sector stemming from a still-restrictive stance of monetary policy (+0.8 percent in 2024 thus far).

New Home Sales*



** The gold bar is a forecast for October 2024.*

Sources: U.S. Census Bureau via Haver Analytics; Daiwa Capital Markets America

Consumer Confidence*

** The gold bar is a forecast for November 2024.*

Sources: The Conference Board via Haver Analytics; Daiwa Capital Markets America

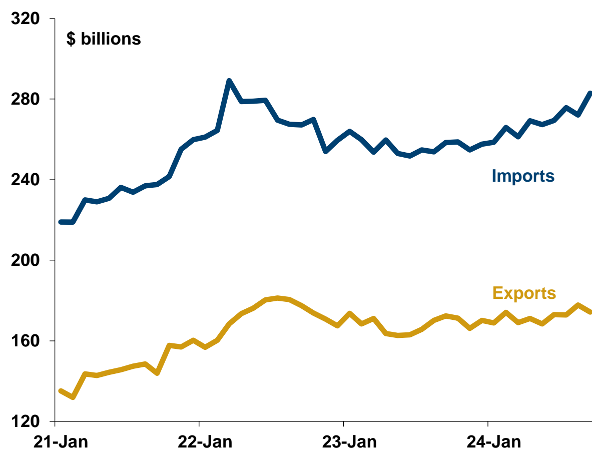
New Orders for Durable Goods

Source: U.S. Census Bureau via Haver Analytics

International Trade in Goods (October) (Wednesday)
Forecast: $101.0 Billion ($7.7 Billion Narrower Deficit)

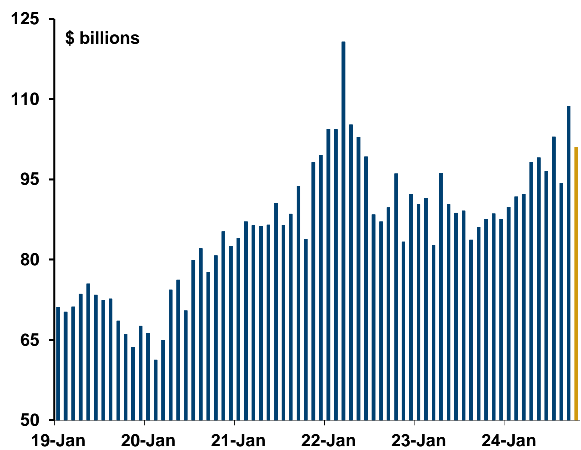
Trade flows are often volatile from month to month, with exports of goods dropping 1.9 percent in September (Census basis) while imports advanced 4.0 percent. Nonetheless, firm underlying demand in the U.S. has supported steady growth in imports while a strong foreign exchange value of the dollar and the sluggish economies of major trading partners have led to a mixed performance in exports. With that said, the surge in imports for September occurred ahead of the early October port strike, as firms possibly accelerated shipping schedules to avoid potential disruptions. Thus, with conditions returning to normal, at least a partial reversion in import flows seems in order for October, which could lead to a narrowing in the deficit.

Total Imports & Exports of Goods



Source: U.S. Census Bureau via Haver Analytics

Nominal Trade Deficit in Goods*



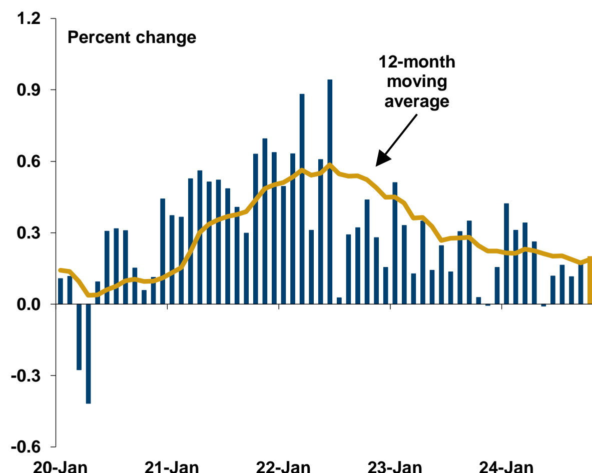
** The gold bar is a forecast for October 2024.*

Sources: U.S. Census Bureau via Haver Analytics; Daiwa Capital Markets America

Personal Income, Consumption, Price Indexes (October) (Wednesday)
Forecast: 0.3% Income, 0.4% Consumption, 0.2% Headline, 0.3% Core

An advance of 0.4 percent in average hourly earnings suggests a favorable performance in overall income growth in October. On the spending side, mixed results in the retail sales reports suggests a light increase in outlays for nondurable items. However, a favorable performance in vehicle sales raises the prospect of a firm reading on outlays for durable goods. Spending on services has remained on a solid track in 2024 thus far. Results for the CPI and PPI suggest increases of 0.2 percent for the headline PCE price index and 0.3 percent for the core. The projected readings would translate to year-over-year advances of 2.3 percent for the headline (versus 2.1 percent in September) and 2.8 percent for the core index (versus 2.7 percent in September).

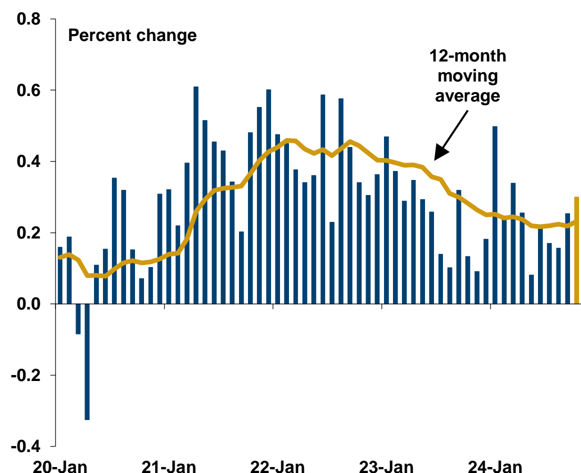
Headline PCE Price Index*



** The gold bar is a forecast for October 2024.*

Sources: Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

Core PCE Price Index*



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Sources: Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

Economic Indicators

November/December 2024

Monday 18

NAHB HOUSING INDEX

Sep	41
Oct	43
Nov	46

TIC FLOWS

	Long-Term	Total
July	$137.9B	$159.1B
Aug	$108.8B	$75.9B
Sep	$216.1B	$398.4B

Tuesday 19

HOUSING STARTS

Aug	1.379 million
Sep	1.353 million
Oct	1.311 million

Wednesday 20

Thursday 21

UNEMPLOYMENT CLAIMS

	Initial (millions)	Continuing
Oct 26	0.218	1.884
Nov 2	0.221	1.872
Nov 9	0.219	1.908
Nov 16	0.213	N/A

PHILADELPHIA FED MFG BUSINESS OUTLOOK

Sep	1.7
Oct	10.3
Nov	-5.5

EXISTING HOME SALES

Aug	3.880 million
Sep	3.830 million
Oct	3.960 million

LEADING INDICATORS

Aug	-0.3%
Sep	-0.3%
Oct	-0.4%

Friday 22

REVISED CONSUMER SENTIMENT

Oct	70.5
Nov(p)	73.0
Nov(r)	71.8

Monday 25

CHICAGO FED NATIONAL ACTIVITY INDEX (8:30)

	Monthly	3-Mo. Avg.
Aug	-0.01	-0.14
Sep	-0.28	-0.19
Oct	--	--

Tuesday 26

FHFA HOME PRICE INDEX (9:00)

July	0.2%
Aug	0.3%
Sep	--

S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX (9:00)

July	0.2%
Aug	0.4%
Sep	--

NEW HOME SALES (10:00)

Aug	0.709 million
Sep	0.738 million
Oct	**0.720 million**

CONFERENCE BOARD CONSUMER CONFIDENCE (10:00)

Sep	99.2
Oct	108.7
Nov	**113.0**

FOMC MINUTES (2:00)

Wednesday 27

UNEMP. CLAIMS (8:30)

GDP (8:30)

	GDP	Chained Price
24-Q2	3.0%	2.5%
24-Q3(a)	2.8%	1.8%
24-Q3(p)	**2.8%**	**1.8%**

DURABLE GOODS ORDERS (8:30)

Aug	-0.9%
Sep	-0.7%
Oct	**1.0%**

INTERNATIONAL TRADE IN GOODS (8:30)

Aug	-$94.2 billion
Sep	-$108.7 billion
Oct	**-$101.0 billion**

ADVANCE INVENTORIES (8:30)

	Wholesale	Retail
Aug	0.2%	0.8%
Sep	-0.2%	0.9%
Oct	--	--

PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX (10:00)

	Inc.	Cons.	Core
Aug	0.2%	0.3%	0.2%
Sep	0.3%	0.5%	0.3%
Oct	**0.3%**	**0.4%**	**0.3%**

PENDING HOME SALES (10:00)

Aug	0.6%
Sep	7.4%
Oct	--

Thursday 28

THANKSGIVING

Friday 29

MNI CHICAGO BUSINESS BAROMETER (9:45)

	Index	Prices
Sep	46.6	74.3
Oct	41.6	67.3
Nov	--	--

Monday 2

ISM MFG. INDEX

CONSTRUCTION

Tuesday 3

JOLTS DATA

VEHICLE SALES

Wednesday 4

ADP EMPLOYMENT

ISM SERVICES INDEX

FACTORY ORDERS

BEIGE BOOK

Thursday 5

UNEMP. CLAIMS

TRADE BALANCE

Friday 6

EMPLOYMENT REPORT

CONSUMER SENTIMENT

CONSUMER CREDIT

Monday 9

WHOLESALE TRADE

Tuesday 10

NFIB SMALL BUSINESS OPTIMISM INDEX

REVISED PRODUCTIVITY & COSTS

Wednesday 11

CPI

FEDERAL BUDGET

Thursday 12

UNEMP. CLAIMS

PPI

Friday 13

IMPORT/EXPORT PRICES

Forecasts in bold. (a) = advance (1st estimate of GDP), (p) = preliminary (2nd estimate of GDP), (r) = revised

Treasury Financing

November/December 2024

Monday	Tuesday	Wednesday	Thursday	Friday
18	19	20	21	22
AUCTION RESULTS: Rate / Cover 13-week bills 4.420% 2.68 26-week bills 4.310% 2.87	**AUCTION RESULTS:** Rate / Cover 42-day CMBs 4.480% 2.55 **ANNOUNCE:** $64 billion 17-week bills for auction on Nov 20 $95 billion 4-week bills for auction on Nov 21 $90 billion 8-week bills for auction on Nov 21 **SETTLE:** $64 billion 17-week bills $95 billion 4-week bills $90 billion 8-week bills	**AUCTION RESULTS:** Rate / Cover 17-week bills 4.380% 3.14 20-yr bonds 4.680% 2.34 40-day CMBs 4.515% 3.87	**AUCTION RESULTS:** Rate / Cover 4-week bills 4.530% 2.68 8-week bills 4.480% 2.52 10-yr TIPS 2.071% 2.35 **ANNOUNCE:** $153 billion 13-,26-week bills for auction on Nov 25 $48 billion 52-week bills for auction on Nov 26 $69 billion 2-year notes for auction on Nov 25 $70 billion 5-year notes for auction on Nov 26 $44 billion 7-year notes for auction on Nov 27 $28 billion 2-year FRNs for auction on Nov 26 $40 billion 30-day CMBs for auction on Nov 25 $80 billion 41-day CMBs for auction on Nov 26	**SETTLE:** $153 billion 13-,26-week bills $80 billion 42-day CMBs $50 billion 40-day CMBs
25	26	27	28	29
AUCTION: $153 billion 13-,26-week bills $69 billion 2-year notes $40 billion 30-day CMBs	**AUCTION:** $48 billion 52-week bills $70 billion 5-year notes $28 billion 2-year FRNs $80 billion 41-day CMBs **ANNOUNCE:** $64 billion* 17-week bills for auction on Nov 27 $95 billion* 4-week bills for auction on Nov 27 $90 billion* 8-week bills for auction on Nov 27 **SETTLE:** $64 billion 17-week bills $95 billion 4-week bills $90 billion 8-week bills $40 billion 30-day CMBs	**AUCTION:** $64 billion* 17-week bills $95 billion* 4-week bills $90 billion* 8-week bills $44 billion 7-year notes **ANNOUNCE:** $153 billion* 13-,26-week bills for auction on Dec 2	***THANKSGIVING***	**SETTLE:** $153 billion 13-,26-week bills $48 billion 52-week bills $17 billion 10-year TIPS $28 billion 2-year FRNs $80 billion 41-day CMBs
2	3	4	5	6
AUCTION: $153 billion* 13-,26-week bills **SETTLE:** $16 billion 20-year bonds $69 billion 2-year notes $70 billion 5-year notes $44 billion 7-year notes	**ANNOUNCE:** $64 billion* 17-week bills for auction on Dec 4 $95 billion* 4-week bills for auction on Dec 5 $90 billion* 8-week bills for auction on Dec 5 **SETTLE:** $64 billion* 17-week bills $95 billion* 4-week bills $90 billion* 8-week bills	**AUCTION:** $64 billion* 17-week bills	**AUCTION:** $95 billion* 4-week bills $90 billion* 8-week bills **ANNOUNCE:** $153 billion* 13-,26-week bills for auction on Dec 9 $58 billion* 3-year notes for auction on Dec 10 $39 billion* 10-year notes for auction on Dec 11 $22 billion* 30-year bonds for auction on Dec 12 **SETTLE:** $153 billion* 13-,26-week bills	
9	10	11	12	13
AUCTION: $153 billion* 13-,26-week bills	**AUCTION:** $58 billion* 3-year notes **ANNOUNCE:** $64 billion* 17-week bills for auction on Dec 11 $95 billion* 4-week bills for auction on Dec 12 $90 billion* 8-week bills for auction on Dec 12 **SETTLE:** $64 billion* 17-week bills $95 billion* 4-week bills $90 billion* 8-week bills	**AUCTION:** $64 billion* 17-week bills $39 billion* 10-year notes	**AUCTION:** $95 billion* 4-week bills $90 billion* 8-week bills $22 billion* 30-year bonds **ANNOUNCE:** $153 billion* 13-,26-week bills for auction on Dec 16 $13 billion* 20-year bonds for auction on Dec 17 $22 billion* 5-year TIPS for auction on Dec 19 **SETTLE:** $153 billion* 13-,26-week bills	

**Estimate*