

1 May 2024

Research US

Fed review – Maintaining easing bias

- **The Fed maintained rates unchanged as widely expected. QT pace for UST holdings will be reduced to USD25bn per month from June, largely as expected.**
- **Powell provided few new clues on the policy outlook, but emphasized that the Fed continues to see its policy having a restrictive effect on demand. We still see rate cuts looming in the horizon earlier than what the markets are pricing in.**
- **Initial dovish market reaction mostly faded after the press conference, with EUR/USD and 10y UST yields little changed from pre-meeting levels. Cumulative pricing for cuts by December rose from around 28bp to 34bp.**

Powell made it clear that the Fed remains in a good place with its current policy. Further disinflation is still in the cards as price pressures from tight labour markets and housing continue easing, even if Q1 data weighed on the confidence surrounding the outlook. Powell did not see recent inflation prints as a sign of demand growth reaccelerating and downplayed the significance of easing seen in financial conditions since last fall, saying that there has been ‘no obvious connection’ between the two.

Powell was asked several times about the possibility of new rate hikes, but he avoided the speculation entirely, sparking a modest dovish reaction in the markets. The pricing of cumulative cuts by December rose from around 28bp to 34bp.

Powell outlined two paths to reducing rates, one where the Fed gains greater confidence in inflation returning to target and second where labour markets weaken unexpectedly. We don’t foresee sharp declines in activity, but still expect to see some further weakening in cyclical indicators and also a modest rise in unemployment rate.

Earlier today, the March JOLTs report showed that the ratio of job openings to unemployed job seekers declined to 1.32 (from 1.36), which is the lowest level since the initial Covid-shock and only marginally above typical pre-pandemic levels (Chart 1). Lower job openings have been a strong leading indicator for lower wage pressures. April ISM Manufacturing index showed that firms’ order-inventory balances have started to weaken in line with signals from the PMIs, pointing towards weaker output growth (Chart 2).

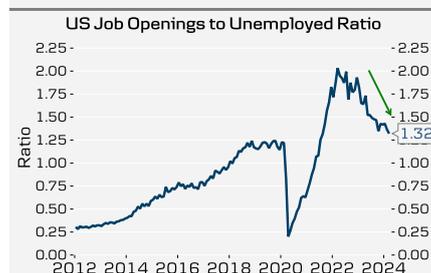
The Fed also announced tapering of the pace of QT, as we discussed in our last week’s *RtM USD*, 23 April. The Fed’s UST holdings will be reduced at a pace of USD25bn per month starting from June (Our forecast: USD30bn, previously USD60bn), while the cap on reducing MBS holdings will be maintained unchanged at USD35bn (as expected). The communication was largely in line with discussion seen in the March minutes, and Powell emphasized that the change was not intended to ease monetary policy stance. In our view, the Fed is likely to continue reducing the size of its balance sheet well into 2025.

To summarize, we have been calling for three 25bp rate cuts in 2024, starting from June. While nothing in Powell’s comments heard today made us less confident in our view, we are currently evaluating the call in light of recent data, and will discuss possible revisions next week after April NFP data.

Our Fed call summarized

- Quarterly 25bp rate cuts from June 2024, as nominal rates are adjusted to slower inflation.
- QT continues past the first rate cut, likely well into 2025

Chart 1: Powell emphasized that the Fed still sees labour demand cooling



Sources: Macrobond Financial, U. S. Bureau of Labor Statistics

Chart 2: Leading indicators point towards weakening output growth as support from inventory cycle fades



Sources: Macrobond Financial, ISM, S&P Global

Senior Analyst, US Macro
Antti Ilvonen
+358 445 180 297
antti.ilvonen@danskebank.com

Disclosures

This research report has been prepared by Danske Bank A/S ('Danske Bank').

Analyst certification

Each research analyst responsible for the content of this research report certifies that the views expressed in the research report accurately reflect the research analyst's personal view about the financial instruments and issues covered by the research report. Each responsible research analyst further certifies that no part of the compensation of the research analyst was, is or will be, directly or indirectly, related to the specific recommendations expressed in the research report.

Regulation

Danske Bank is authorised and regulated by the Danish Financial Services Authority (Finanstilsynet). Danske Bank is authorised by the Prudential Regulation Authority in the UK. Subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request.

Danske Bank's research reports are prepared in accordance with the recommendations of Capital Market Denmark.

Conflicts of interest

Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high-quality research based on research objectivity and independence. These procedures are documented in Danske Bank's research policies. Employees within Danske Bank's Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and the Compliance Department. Danske Bank's Research Departments are organised independently from, and do not report to, other business areas within Danske Bank.

Research analysts are remunerated in part based on the overall profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.

Financial models and/or methodology used in this research report

Calculations and presentations in this research report are based on standard econometric tools and methodology as well as publicly available statistics for each individual security, issuer and/or country. Documentation can be obtained from the authors on request.

Risk warning

Major risks connected with recommendations or opinions in this research report, including as sensitivity analysis of relevant assumptions, are stated throughout the text.

Expected updates

Ad hoc

Date of first publication

See the front page of this research report for the date of first publication.

General disclaimer

This research has been prepared by Danske Bank A/S. It is provided for informational purposes only and should not be considered investment, legal or tax advice. It does not constitute or form part of, and shall under no circumstances be considered as, an offer to sell or a solicitation of an offer to purchase or sell any relevant financial instruments (i.e. financial instruments mentioned herein or other financial instruments of any issuer mentioned herein and/or options, warrants, rights or other interests with respect to any such financial instruments) ('Relevant Financial Instruments').

This research report has been prepared independently and solely on the basis of publicly available information that Danske Bank A/S considers to be reliable but Danske Bank A/S has not independently verified the contents hereof. While reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation or warranty, express or implied, is made as to, and no reliance should be placed on, the fairness, accuracy, completeness or reasonableness of the information, opinions and projections contained in this research report and Danske Bank A/S, its affiliates and subsidiaries accept no liability whatsoever for any direct or consequential loss, including without limitation any loss of profits, arising from reliance on this research report.

The opinions expressed herein are the opinions of the research analysts and reflect their opinion as of the date hereof. These opinions are subject to change and Danske Bank A/S does not undertake to notify any recipient of this research report of any such change nor of any other changes related to the information provided in this research report.

This research report is not intended for, and may not be redistributed to, retail customers in the United Kingdom (see separate disclaimer below) and retail customers in the European Economic Area as defined by Directive 2014/65/EU.

This research report is protected by copyright and is intended solely for the designated addressee. It may not be reproduced or distributed, in whole or in part, by any recipient for any purpose without Danske Bank A/S's prior written consent.

Disclaimer related to distribution in the United States

This research report was created by Danske Bank A/S and is distributed in the United States by Danske Markets Inc., a U.S. registered broker-dealer and subsidiary of Danske Bank A/S, pursuant to SEC Rule 15a-6 and related interpretations issued by the U.S. Securities and Exchange Commission. The research report is intended for distribution in the United States solely to 'U.S. institutional investors' as defined in SEC Rule 15a-6. Danske Markets Inc. accepts responsibility for this research report in connection with distribution in the United States solely to 'U.S. institutional investors'.

Danske Bank A/S is not subject to U.S. rules with regard to the preparation of research reports and the independence of research analysts. In addition, the research analysts of Danske Bank A/S who have prepared this research report are not registered or qualified as research analysts with the New York Stock Exchange or Financial Industry Regulatory Authority but satisfy the applicable requirements of a non-U.S. jurisdiction.

Any U.S. investor recipient of this research report who wishes to purchase or sell any Relevant Financial Instrument may do so only by contacting Danske Markets Inc. directly and should be aware that investing in non-U.S. financial instruments may entail certain risks. Financial instruments of non-U.S. issuers may not be registered with the U.S. Securities and Exchange Commission and may not be subject to the reporting and auditing standards of the U.S. Securities and Exchange Commission.

Disclaimer related to distribution in the United Kingdom

In the United Kingdom, this document is for distribution only to (I) persons who have professional experience in matters relating to investments falling within article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the 'Order'); (II) high net worth entities falling within article 49(2)(a) to (d) of the Order; or (III) persons who are an elective professional client or a per se professional client under Chapter 3 of the FCA Conduct of Business Sourcebook (all such persons together being referred to as 'Relevant Persons'). In the United Kingdom, this document is directed only at Relevant Persons, and other persons should not act or rely on this document or any of its contents.

Disclaimer related to distribution in the European Economic Area

This document is being distributed to and is directed only at persons in member states of the European Economic Area ('EEA') who are 'Qualified Investors' within the meaning of Article 2(e) of the Prospectus Regulation (Regulation (EU) 2017/1129) ('Qualified Investors'). Any person in the EEA who receives this document will be deemed to have represented and agreed that it is a Qualified Investor. Any such recipient will also be deemed to have represented and agreed that it has not received this document on behalf of persons in the EEA other than Qualified Investors or persons in the UK and member states (where equivalent legislation exists) for whom the investor has authority to make decisions on a wholly discretionary basis. Danske Bank A/S will rely on the truth and accuracy of the foregoing representations and agreements. Any person in the EEA who is not a Qualified Investor should not act or rely on this document or any of its contents.

Report completed: 1 May 2024, 22:45 CET

Report first disseminated: 1 May 2024, 22:55 CET