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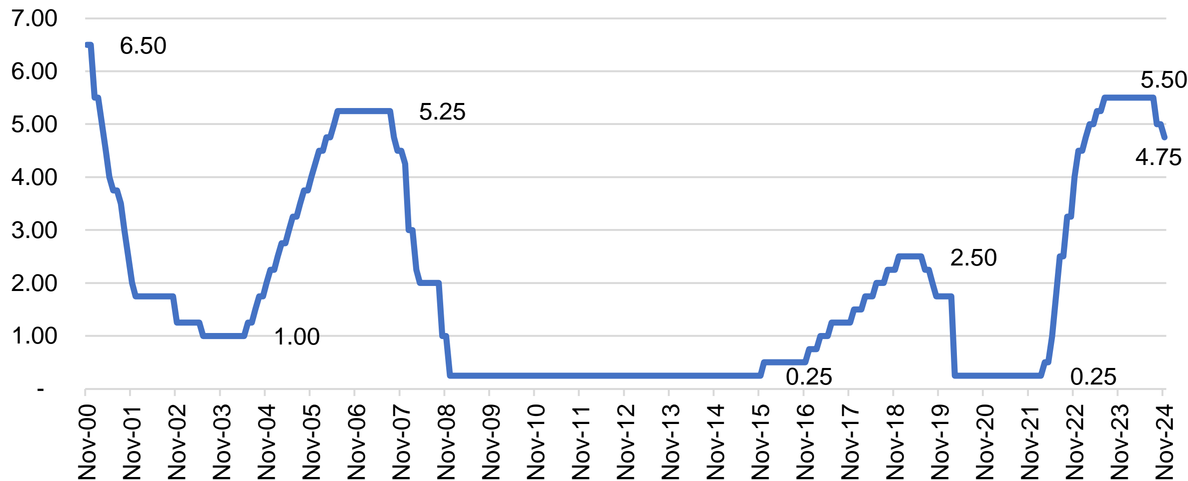
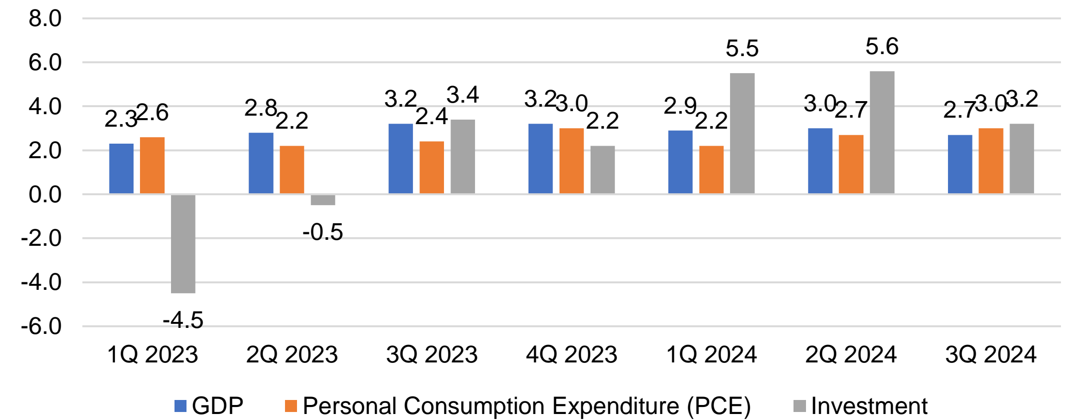
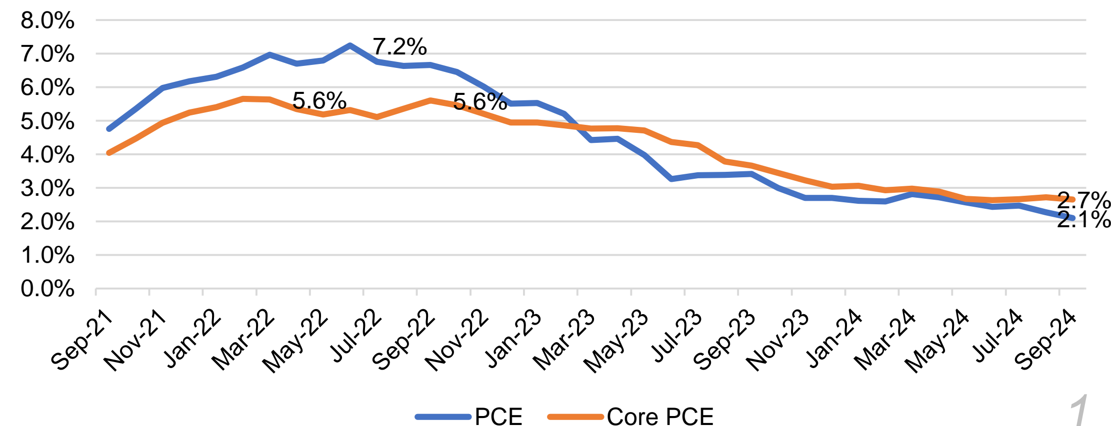
8 NOVEMBER 2024

The Fed cut the interest rates again.



The Federal Open Market Committee (FOMC) unanimously voted to lower the Federal Funds Rate (FFR) by 25 basis points, shifting it from the previous range of 4.75% - 5.00% to 4.50% - 4.75%. According to the FOMC statement, the committee views the U.S. economy as performing strongly, with continued solid growth. However, the labor market has shown signs of cooling, with Nonfarm Payroll (NFP) averaging 104.3k from August to October this year, compared to a year-to-date average of 170k. Additionally, inflation is progressing in line with the Fed's 2.0% target. Consequently, the Fed has adjusted its restrictive stance, suggesting a shift toward a more neutral monetary approach going forward.





Sources: Bureau of Economic Analysis (BEA), Bureau of Labor Statistics (BLS) & Bloomberg

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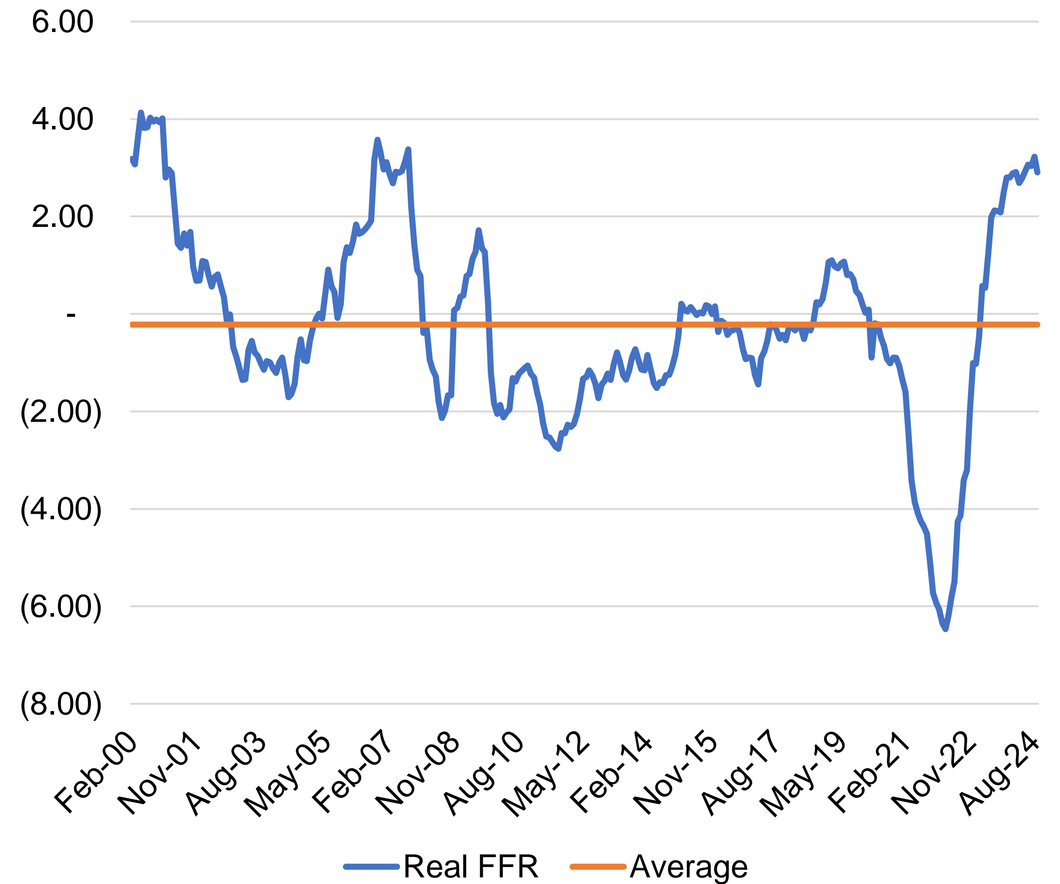
The FFR is still in the restrictive zone

The real Federal Funds Rate (FFR), calculated by subtracting the inflation rate from the nominal FFR, stands at 2.91% as of September, significantly above the historical average of –0.22% since 2000. This indicates that borrowing costs are relatively high in real terms, factoring in inflation. As a result, debt servicing has become more challenging, as evidenced by the rise in delinquency rates across the banking sector.

Total delinquency rates have increased to 1.49% as of 2Q 2024, up from 1.26% in the same period last year. Consumer delinquencies, crucial since consumer spending accounts for two-thirds of U.S. GDP, have also accelerated from 2.38% in 2Q 2023 to 2.74% in 2Q 2024. Specifically, credit card delinquencies climbed from 2.77% in 2Q 2023 to 3.25% in 2Q 2024.

These trends strengthen the case for a potential FFR reduction as the Fed may need to prioritize its dual mandate of maximum employment. According to the Fed's September projections, the FFR is expected to be around 4.4% in 2024, 3.4% in 2025, and 2.9% in 2026, suggesting a gradual shift toward a neutral stance. However, the Fed emphasized that the FOMC's course is not predetermined, with decisions contingent on incoming data and government policy adjustments.



Source: CEIC

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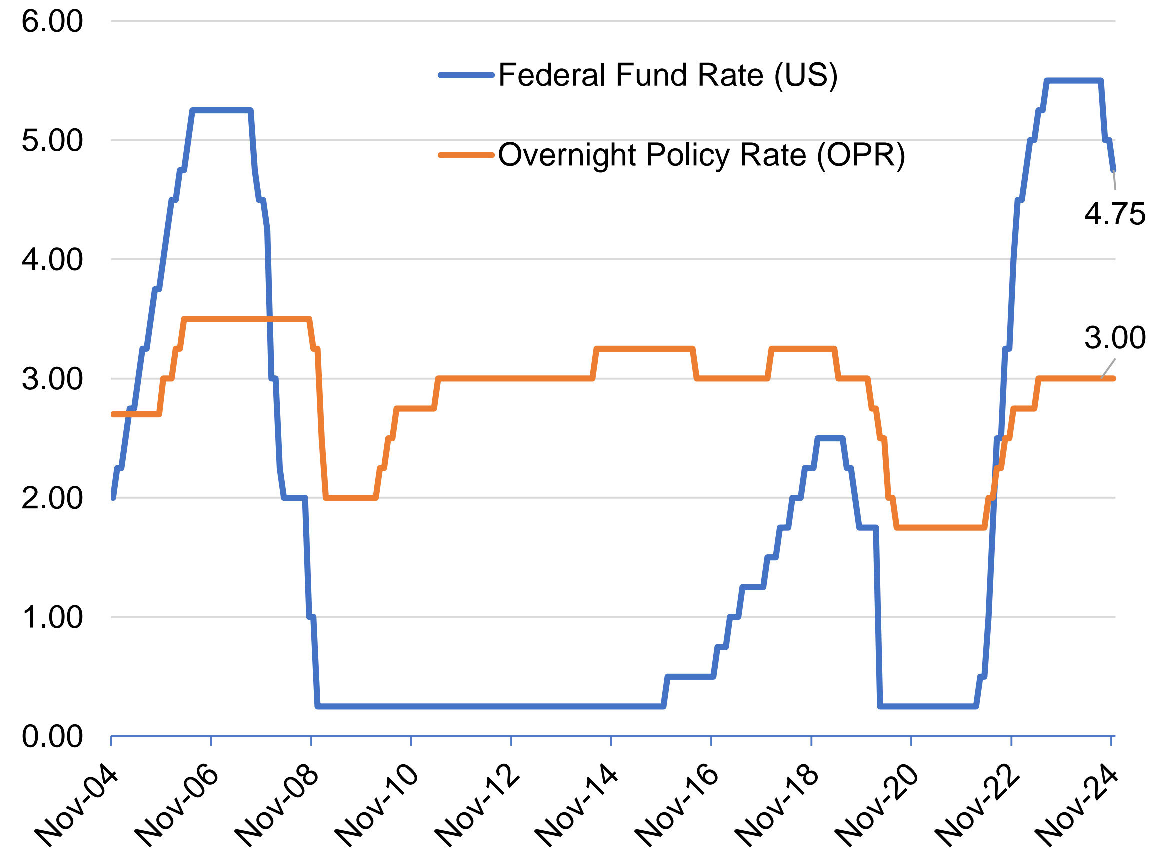
Will BNM follow suit?

The Federal Reserve undeniably sets the trend in monetary policy, making its actions one of the most closely watched events globally. Its decisions heavily influence the bond market, with bond yields often reacting in anticipation of Fed moves. Broadly, global interest rates have reached their peak, and several regions have begun lowering their benchmark rates. Thus, it's reasonable to conclude that global interest rates are on a downward path.

In Malaysia, however, Bank Negara Malaysia (BNM) has highlighted its primary focus on policy shifts, particularly the anticipated rationalization of the RON95 fuel subsidy, set to occur mid-2025. The Malaysian government projects an inflation rate between 2.0% and 3.5% for 2025, up from an estimated 1.5% to 2.0% in 2024, largely driven by the expected rise in fuel prices next year.

As a result, BNM is likely to maintain its current policy stance in 2025, awaiting the adjustment in RON95 prices and the effectiveness of government mitigation measures.



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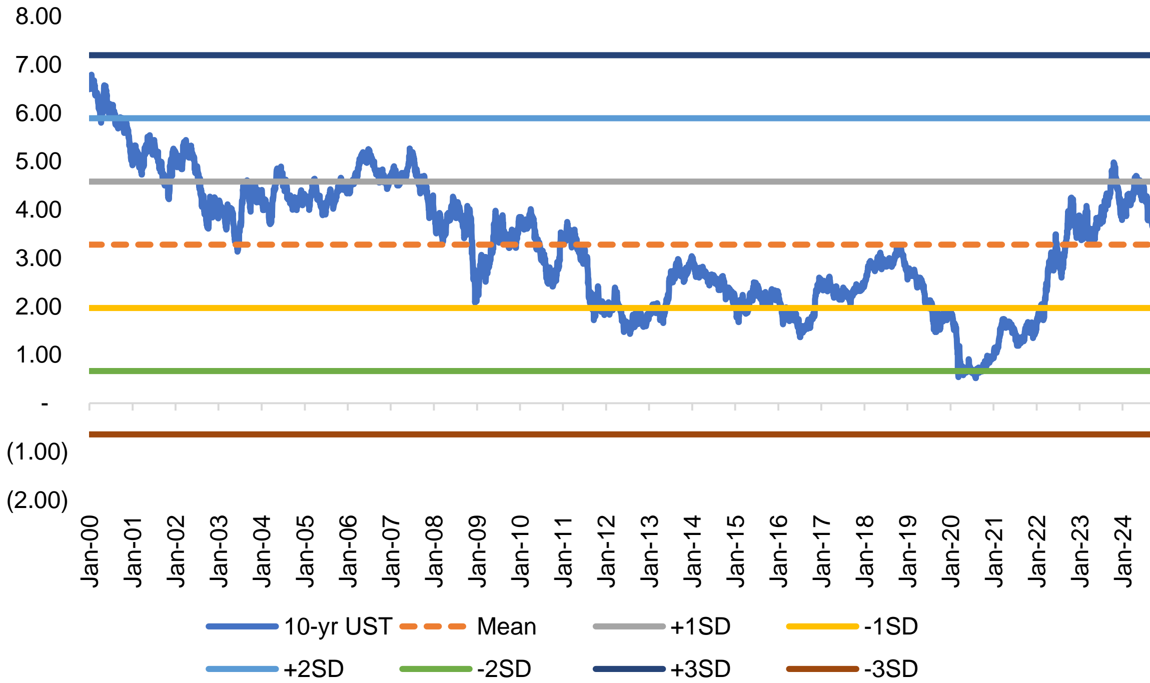
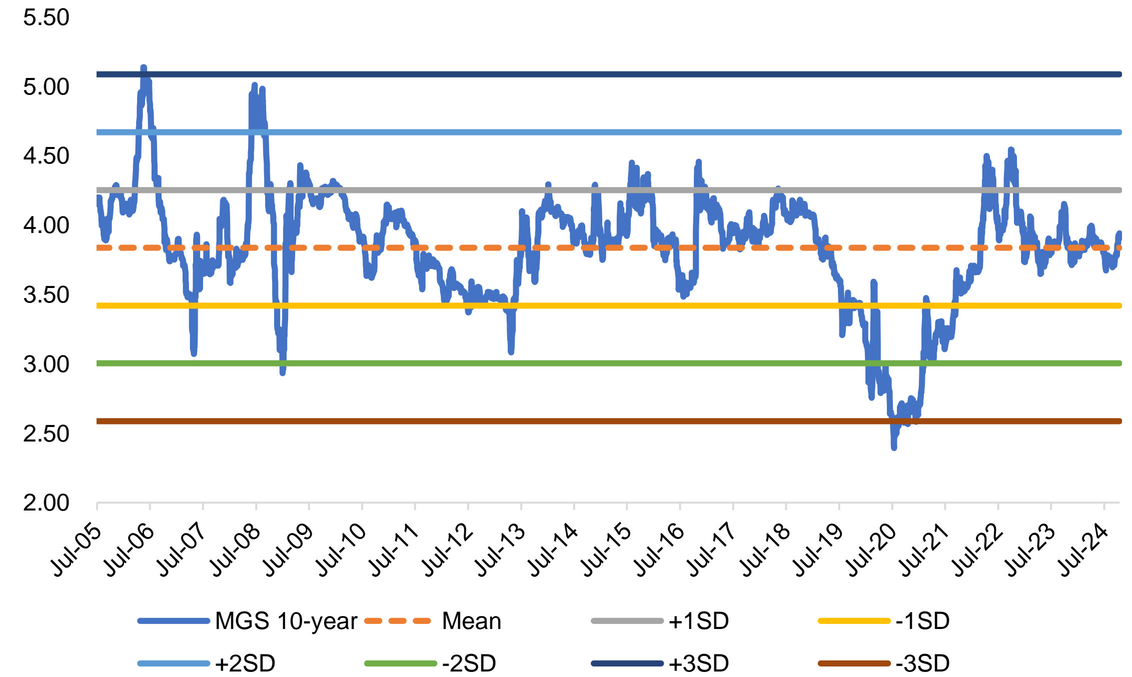
Bond yields could go lower





Source: CEIC

Currently, the 10-year U.S. Treasury (UST) yield stands at 4.35%, significantly above its long-term average of 3.28%. Given the Fed's anticipated shift towards monetary easing in 2025, there is a strong likelihood that the 10-year UST yield will decrease, potentially settling within a range of 3.60% to 4.00% in 2025. Meanwhile, the 10-year Malaysian Government Securities (MGS) yield is trading at 3.92%, slightly above its long-term average of 3.84%. We expect the 10-year MGS yield to ease as well, likely moving between 3.70% and 3.80% in 2025.

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