Financial Markets This Week

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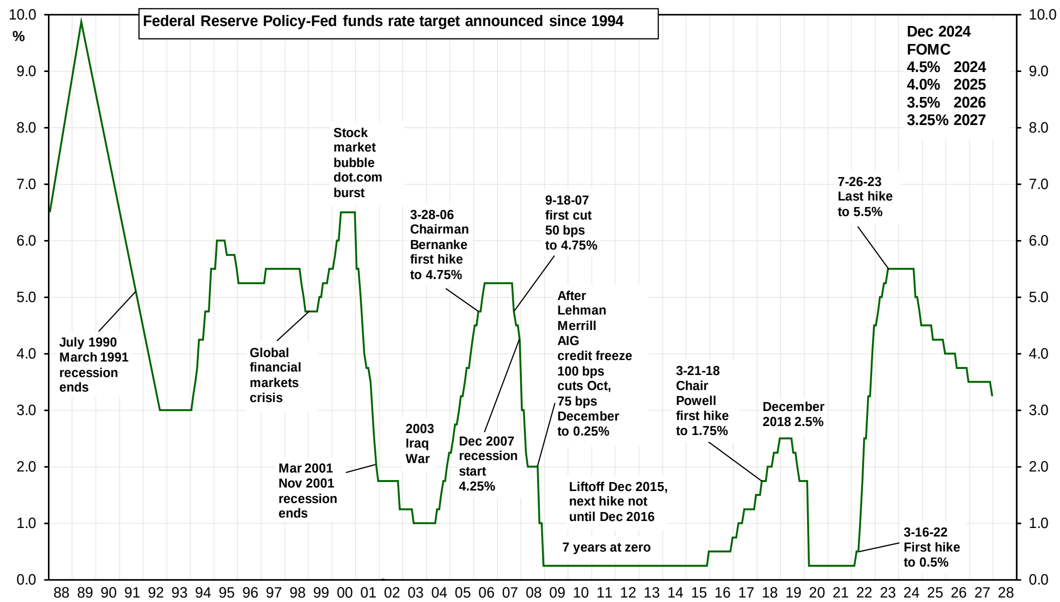
Christopher S. Rupkey, CFA
Chief Economist
crupkey@fwdbonds.com

2025 TWO CUTS NOT FOUR

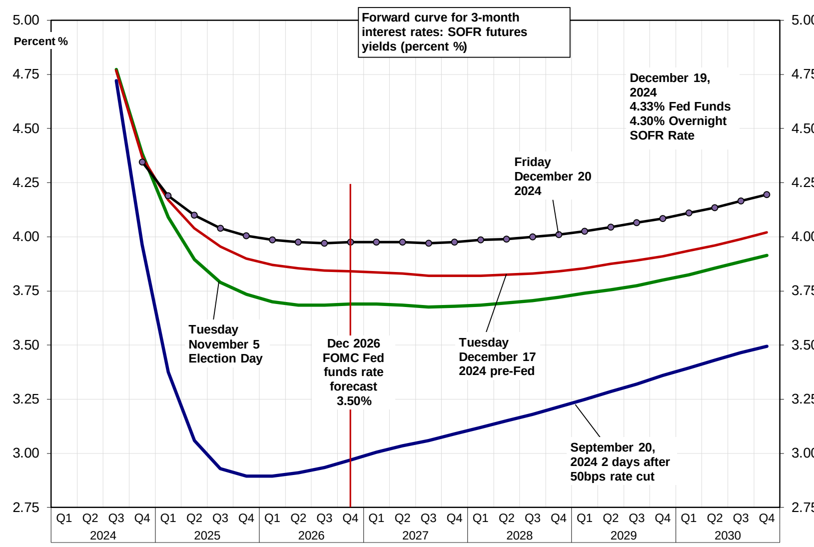


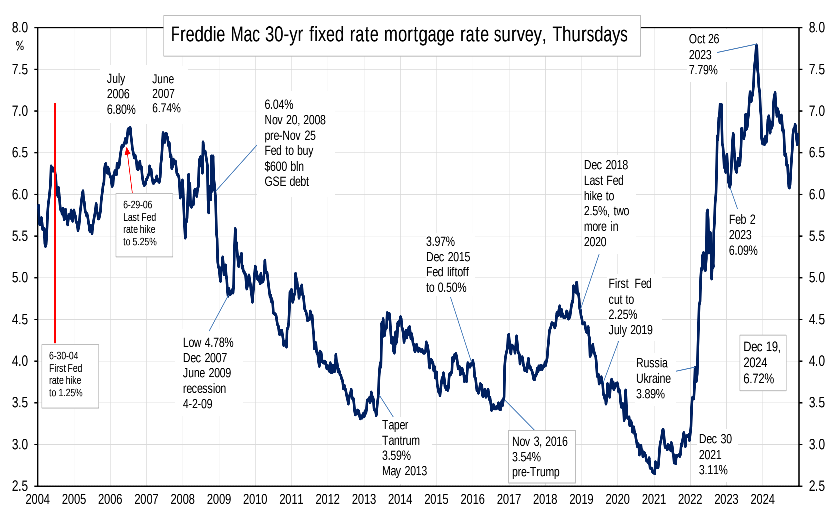
Wherever you were, whatever you thought when you heard the Fed news Wednesday, the S&P 500 collapse by the close tells you all you need to know. The S&P 500 fell 2.9%,the biggest drop after a Fed meeting since March 2020 during the start of the pandemic. Market did not like what the Fed did on Wednesday, although surely, investors must have guessed the Fed rate cuts in 2025 could be pared back to two instead of the old forecast of four. We have to say that two rate cuts by December 2025 makes it hard for markets to discount exactly when the rate cuts might occur, so there is considerable uncertainty. There are eight meetings a year. Four rate cuts in a year, like the September 2024 forecast, are easier to account for; just cut every end of the quarter meeting when you publish your forecasts. Forecasting a rate cut in June and then the other one in December 2025 does not make any sense. We'll just have to go meeting to meeting and follow the bouncing ball of Fed funds futures. Core PCE inflation is 2.8% year-year in October 2024, and if it comes closer to the 2.5% Q4 2025 FOMC forecast, maybe a rate cut is in order, assuming there is no chaos from Washington to upset the economy's applecart. The other wildcard for Fed rate cuts being brought forward, besides what the president-elect thinks, is the labor market and Powell again said at the press conference they did not think the jobs market needed to weaken further to bring inflation down to 2.0% target. The Fed forecasts do not look for the unemployment rate to rise above 4.3%. Remember it was the two-tenths jump in July unemployment to 4.3% on August 2, 2024 that helped pave the way for Powell's first rate cut of an oversized 50 bps.

Fed Policy-key variables	2024	2025	2026	2027	Long Term
Fed funds	4.4	3.9	3.4	3.1	3.0
PCE inflation	2.4	2.5	2.1	2.0	2.0
Core inflation	2.8	2.5	2.2	2.0	
Unemployed	4.2	4.3	4.3	4.3	4.2
GDP	2.5	2.1	2.0	1.9	1.8
December 2024 median Fed forecasts					

Fed Individual Forecasts					
Fed funds rate at year-end					Longer
Votes	2024 End	2025 End	2026 End	2027 End	run
1	4.375	3.125	2.375	2.375	2.375
2	4.375	3.375	2.750	2.625	2.500
3	4.375	3.625	2.875	2.750	2.625
4	4.375	3.625	3.125	2.875	2.750
5	4.375	3.625	3.125	2.875	2.875
6	4.375	3.875	3.125	3.125	2.875
7	4.375	3.875	3.125	3.125	2.875
8	4.375	3.875	3.375	3.125	2.875
9	4.375	3.875	3.375	3.125	3.000
10	4.375	3.875	3.375	3.125	3.000
11	4.375	3.875	3.375	3.125	3.000
12	4.375	3.875	3.375	3.125	3.125
13	4.375	3.875	3.625	3.375	3.375
14	4.375	3.875	3.625	3.625	3.500
15	4.375	3.875	3.625	3.625	3.500
16	4.625	4.125	3.625	3.625	3.625
17	4.625	4.125	3.875	3.625	3.625
18	4.625	4.125	3.875	3.875	3.750
19	4.625	4.375	3.875	3.875	3.875
Median	4.375	3.875	3.375	3.125	3.000
Meeting	Dec 24	Dec 24	Dec 24	Dec 24	Dec 24

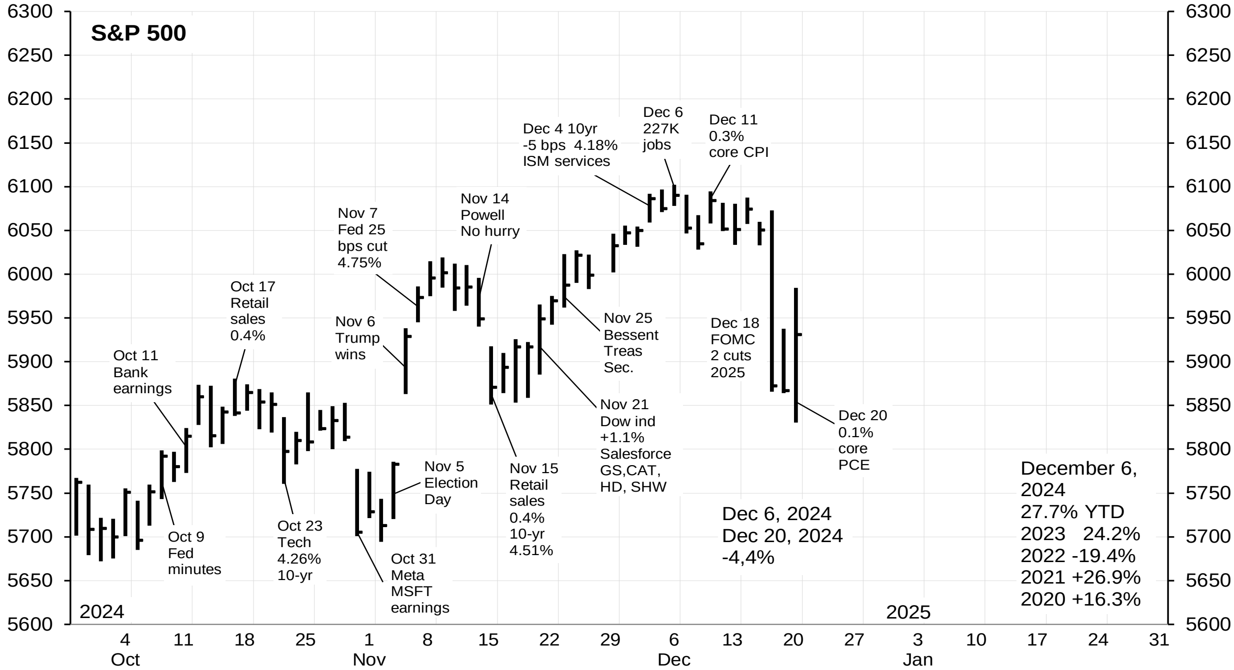
Here was our instant analysis Wednesday: The Federal Reserve met today and after cutting rates 25 bps as expected to 4.5%, they pared back the 2025 25 bps rate cuts to two in number from the four moves they anticipated at the September meeting. They are less confident that inflation will continue to move lower as they have penciled in a 2.5% Q4 2025 core PCE forecast where in September they were more confident with their forecast of core PCE inflation falling to 2.1% at the end of 2025. As far as the eye can see they now anticipate a Fed funds rate of 4.0% in 2025 and 3.5% in 2026 where in September they saw a 3.5% Fed funds rate at the end of next year and 3.0% at the end of 2026. Slow it down is the theme at today's meeting. Although it was interesting their GDP forecast in 2025 is little changed at 2.1% so they are waiting for more details on the president-elect's pro-growth agenda before they up their forecast on economic growth. It is important to note that they are not reversing course on policy, they are still moving interest rates down in 2025, just not at the speed they thought a few months ago. This is bad news for homebuyers because there is little chance that long-term Treasury yields will fall significantly, so mortgage rates will likely remain above 6% for all of next year.





To conclude, it looks like much of the country took a breath after the November election results, and Fed policymakers are taking a breather as well. After cutting rates at three straight meetings, the rate cuts anticipated over the eight meetings in 2025 will be much less frequent, as the president-elect's plans for spending and tax cuts and tariffs associated with his pro-growth agenda risk stopping inflation's move down to target in its tracks. A stronger economy with greater demand produces more inflation, there is simply no way to repeal this economic law of nature. The Fed is taking a wait and see approach to monetary policy easing because all the blustery campaign talk could change from hyperbole to reality in a hurry once the president-elect hits the ground running at the end of January. Historically, most Federal Reserve rate cuts are made either in a recession or economic downturn or in anticipation of one. A 3% GDP growth rate this quarter with core consumer inflation stalled at 2.8% does not cry out for another rate cut to stoke the fires of economic demand to keep the country moving forward to greater prosperity.

INTEREST RATES



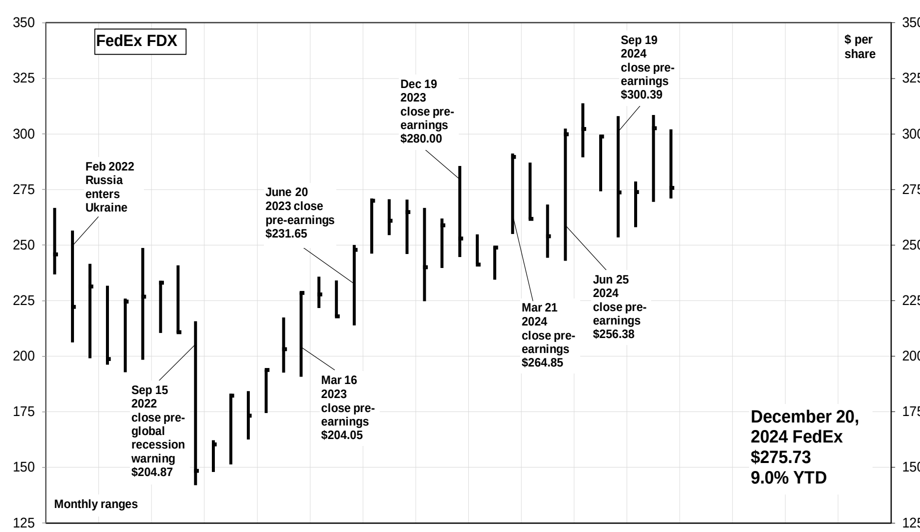
Chaos down in Washington equals chaos in the stock market. The S&P 500 fell as much as 4.4% from the December 6 high to the early Friday morning low. House votes taken to get beyond the 1201am ET Saturday deadline for a Federal government shutdown failed as well and was part of the equity markets fears, but mostly it was the Powell press conference outlining fewer rate cuts in 2025: two cuts ending at 4.0% were forecast versus the September meeting forecast of four cuts and 3.5% Fed rate at the end of 2025. 10-yr Treasury yields moved up as high as 4.60% Thursday afternoon from last week's 4.40% close. The November core PCE inflation reading of 0.1% (0.2e) rallied stocks and bonds, perhaps inflation looking better than the November 0.3% core CPI on December 11. Volume dwindled Friday afternoon: S&P 500 closed Friday up 1.1% had been 2.0% higher intraday.

FedEx (FDX) up 9.0% YTD; S&P 500 up 24.3% YTD

Haywire response to earnings Thursday evening in an admittedly volatile week for the S&P 500 given the news cycle. FedEx was up 7.0% to $295.24 Friday morning before closing -0.1% on the day. Operating earnings for "Federal Express" were okay, the company said, given the headwinds of weak domestic demand and expired US Postal Service contract. FedEx Freight is to be spun out into a new company.

Operating Income $bln

Quarter	Total	Federal Express	FedEx Freight	Other; layoffs
11.30.24	1.052	1.052	0.312	-0.312
8.31.24	1.080	0.953	0.439	-0.312
5.31.24	1.555	1.305	0.507	-0.257
2.29.24	1.243	1.173	0.341	-0.271
11.30.23	1.276	1.035	0.491	-0.250
8.31.23	1.485	1.306	0.482	-0.303



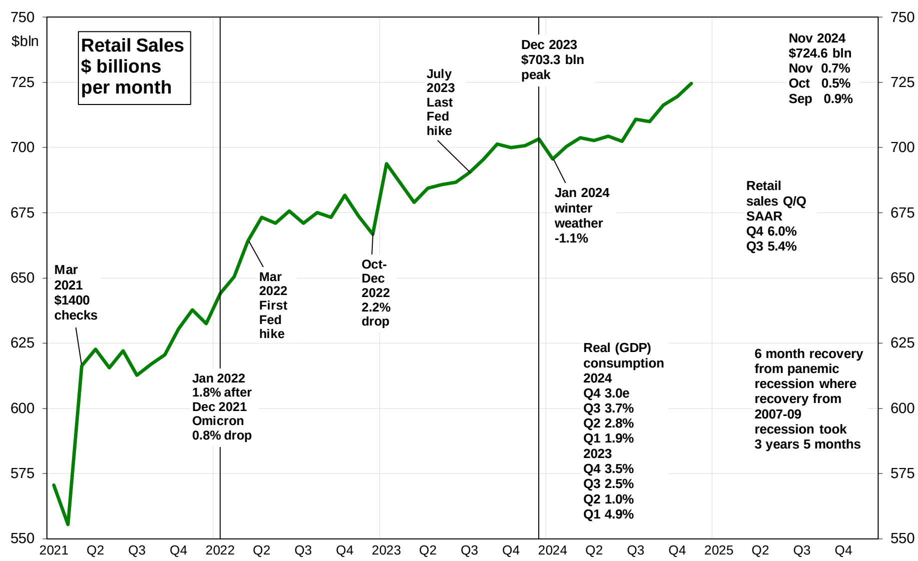
OTHER ECONOMIC NEWS

Retail sales boom (Tuesday)

Retail spending, actual dollars, each month

	$million Nov	% to Total	Percent Changes % Nov	Oct	Year/year
Total Retail Sales	724,609	100.0	0.7	0.5	3.8
Motor vehicles/parts	140,701	19.4	2.6	1.8	6.5
Furniture/furnishings	11,324	1.6	0.3	-0.7	0.7
Electronics/appliances	7,622	1.1	0.3	2.4	1.2
Building materials/garden	42,241	5.8	0.4	0.8	4.1
Food & beverage	83,722	11.6	-0.2	-0.1	1.8
Health/personal care	38,083	5.3	0.0	-1.1	1.8
Gasoline stations	51,502	7.1	0.1	0.1	-3.9
Clothing/accessories	26,318	3.6	-0.2	0.4	2.2
Sporting goods, books	8,296	1.1	0.9	-0.6	-1.4
General merchandise	76,101	10.5	-0.1	0.0	3.1
Department stores	10,818	1.5	-0.6	-0.1	1.4
Miscellaneous retailers	14,910	2.1	-3.5	-0.8	0.8
Nonstore retailers (internet)	127,095	17.5	1.8	0.1	9.8
Eating & drinking places	96,694	13.3	-0.4	0.9	1.9
[Total ex-autos/gas]	532,406	73.5	0.2	0.2	3.9

Breaking economy news. Retail sales were flat for most of the first half of 2024, but no more. Retail sales jumped 0.7% in November and are running 6.0% in the fourth quarter with December data left to be reported. This is one of the rare times when retail sales and real consumption expenditures that go into real GDP are reported (Friday) in the same week. Real consumption spending includes services. The only services item in retail sales are eating and drinking places which fell 0.4% in November following October's 0.9% gain. Motor vehicles have been very strong, up 1.8% in October and now today rising 2.6% in November.



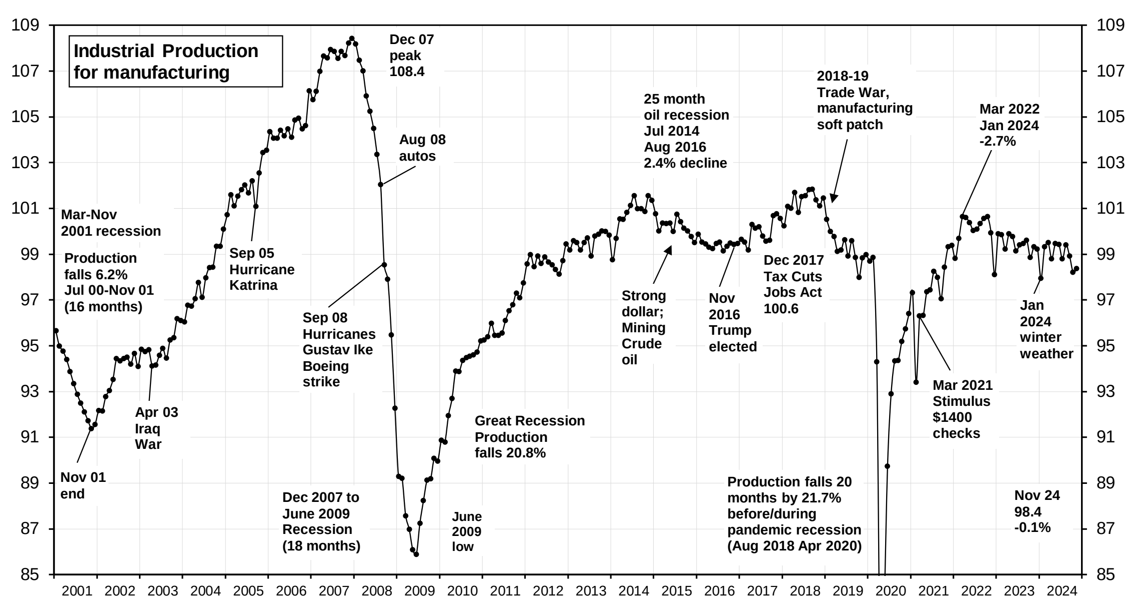
Net, net, the consumer isn't buying the uncertainty outlook, they are out shopping in force sending the economy into the stratosphere this quarter. One of the goals of the incoming administration has already been reached, the economy is growing 3% in the final quarter of 2024 closing out the year with a sign of strength. We have not checked the record books, but the Federal Reserve has probably not cut interest rates to stimulate growth when retail sales are this strong as they are meeting. Maybe it is mostly cars and SUVs this quarter, but it doesn't matter, they've got the cash and they are spending it. From the hurricane hiccup in August where retail sales dropped 0.1%, the consumer is powering the economy ahead at great speed with increases of 0.9% September, 0.5% October, 0.7% November. The market is still discounting a 25 bps rate cut to 4.5% tomorrow, but if consumers are still buying interest-sensitive goods like autos, a rational markets observer would have to wonder why would a central bank add fuel to the fire with a president-elect coming in at the end of January with one of the most pro-growth agendas of any president in history. Stay tuned. Economy what ails ya? Absolutely nothing. It's perfect. Bet on it. There are some troubling proposals from the president-elect to turn the world upside down and bring factories back to the USA, but consumers don't appear to buy these threats, instead they are buying everything else that isn't nailed down or hidden behind lock and key.

Factory production up barely (Tuesday)

Breaking economy news. Also on Tuesday, but released at 915am ET for some reason, the Federal Reserve's industrial production index. Industrial production has fallen three straight months. The October decline had the Boeing strike and Hurricane Milton. The September decline also had the Boeing strike and a couple of hurricanes. Manufacturing industrial production rebounded slightly by 0.2% in November, mostly due to auto output. There is a long way to go to bring manufacturing production back to where it was before the Great Recession. The category of semiconductors, printed circuit boards, and other is up 11.7% from year ago levels, but not enough to bring the total index up.

Percent changes			Industrial Production November 2024		
Sep	Oct	Nov	YOY		Weight
-0.5	-0.4	-0.1	-0.9	Total Index	100.0
-0.5	-0.7	0.2	-1.0	Manufacturing	75.1
-0.7	-0.1	-0.9	-1.3	Mining	14.2
-0.6	1.3	-1.3	0.1	Utilities	10.7
			Manufacturing payroll jobs 12.9 million -61K YOY 9.5% of Private Payroll Jobs		

Net, net, manufacturing can barely keep its head above water so if the incoming administration has some ideas to revitalize the moribund state of factory production, plant managers are all ears. Manufacturing industrial production rose 0.2% in November, but it was one step forward, two steps back with September's and October's losses each revised 0.2% lower. It took decades for US companies to move their operations overseas, and to think one can simply snap their fingers and bring factories back to US shores overnight is a pipedream. Company executives have said time and time again that labor costs are too high in this country, and Wall Street earnings expectations are too great to bring factories back to the US. Labor costs are too high and increasing labor shortages are as well as the native born population in the US is set to decline. Stay tuned. Manufacturing output has made a weak rebound after being depressed due to hurricanes and company strikes, but the future remains uncertain with no company willing to commit to new construction, outside of the semiconductor industry, until they see the full extent of import tariffs proposed by the president-elect.

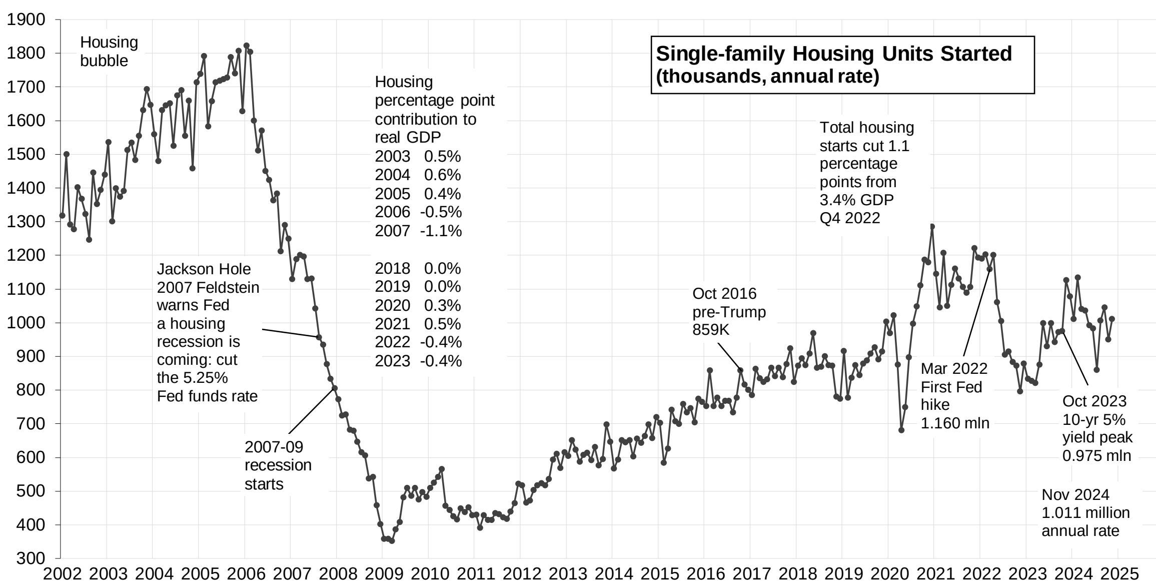


Housing starts down, fewer apartments (Wednesday)

Breaking economy news. One unit housing starts rebounded to 1.011 million in November after falling 9.1% to 950 thousand in October because of Hurricane Milton that hit near Sarasota, Florida. Total housing starts fell however as multifamily was near the weakest of the year.

Housing Starts Total, Single-Family, Multi-Family											
	United States			Northeast		Midwest		South		West	
000s	Total	1 unit	Multi	Total	1 unit	Total	1 unit	Total	1 unit	Total	1 unit
Nov 2024	1289	1011	264	115	46	158	132	727	621	289	212
Oct 2024	1312	950	348	104	60	220	137	660	525	328	228
Nov 2023	1510	1126	371	129	72	203	168	818	631	360	255
% Chgs											
Nov/Oct	-1.8	6.4	...	10.6	-23.3	-28.2	-3.6	10.2	18.3	-11.9	-7.0
Nov/Nov	-14.6	-10.2	...	-10.9	-36.1	-22.2	-21.4	-11.1	-1.6	-19.7	-16.9

Net, net, residential housing construction is mixed in November with multifamily construction getting crushed and dragging down the entire number of housing starts despite a hefty double-digit rebound in single-family starts down South after the hurricanes have passed. Time will tell whether the incoming pro-business administration is going to turn around sentiment of builders, but at the moment, the early read is caution on the part of the housing construction industry. The president-elect has a pro-growth economic agenda, but unless there is some action taken to bring mortgage rates down from 6% to 3% where rates were prior to the massive Fed hikes to curb inflation starting in March 2022, then the housing outlook is unlikely to be a bright one in 2025 despite the changes being talked about down in Washington. Stay tuned.



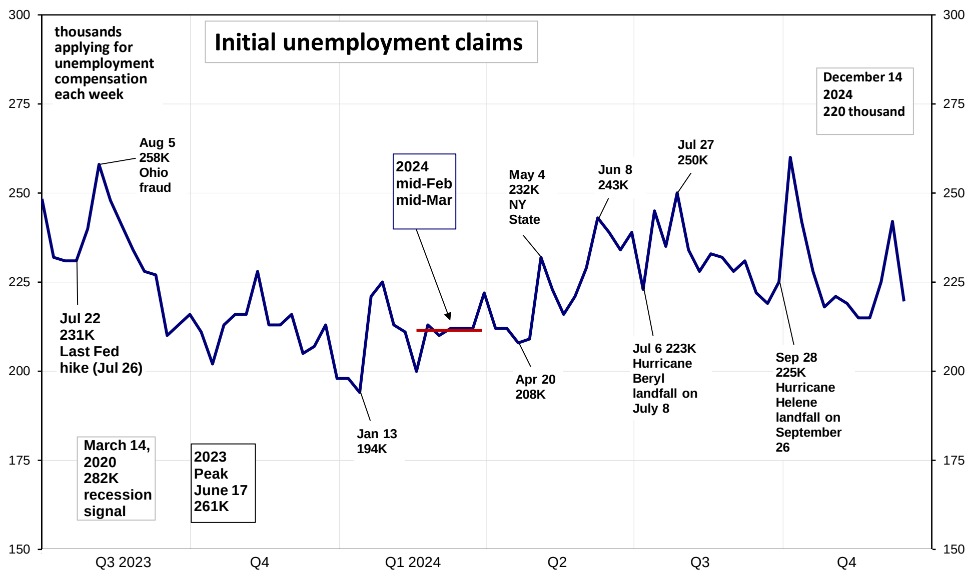
Job layoffs tumble, 3.1% GDP (Friday)

Breaking economy news. Third look at third quarter real GDP showed an upward revision to 3.1% from the second estimate of 2.8%. Exports added a little bit more, maybe not for long if our trading partners retaliate with their own tariffs. Imports subtract 1.4 percentage points, so if we made it all here, that would be a big boost to real domestic product, real GDP. Fanciful speculation however. No expectation this will become a reality. No labor here in the USA for one thing.

	Q2 23	Q3 23	Q4 23	Q1 24	Q2 24	Q3 24p	Q3 24r	Q3 24f
REAL GDP	2.4	4.4	3.2	1.6	3.0	2.8	2.8	3.1
REAL CONSUMPTION	1.0	2.5	3.5	1.9	2.8	3.7	3.5	3.7
CONSUMPTION	0.7	1.7	2.3	1.3	1.9	2.5	2.4	2.5
Durables	0.0	0.3	0.2	-0.1	0.4	0.6	0.5	0.5
Nondurables	-0.1	0.4	0.5	-0.1	0.2	0.7	0.6	0.6
Services	0.7	1.0	1.6	1.6	1.3	1.2	1.2	1.3
INVESTMENT	1.4	1.8	0.2	0.6	1.5	0.1	0.2	0.2
Business Plant	0.5	0.1	0.2	0.2	0.0	-0.1	-0.2	-0.2
& Equipment and	0.6	-0.1	0.0	0.0	0.5	0.6	0.5	0.5
Intellectual Property	0.2	0.2	0.3	0.4	0.0	0.0	0.1	0.2
Homes	0.2	0.3	0.1	0.5	-0.1	-0.2	-0.2	-0.2
Inventories	-0.1	1.3	-0.5	-0.5	1.1	-0.2	-0.1	-0.2
EXPORTS	-0.5	0.5	0.7	0.2	0.1	0.9	0.8	1.0
IMPORTS	0.4	-0.6	-0.6	-0.8	-1.0	-1.5	-1.4	-1.4
GOVERNMENT	0.5	0.9	0.6	0.3	0.5	0.9	0.8	0.9
Federal defense	0.0	0.2	-0.1	-0.1	0.2	0.5	0.5	0.5
Fed nondefense	-0.1	0.1	0.0	0.1	0.0	0.1	0.1	0.1
State and local	0.6	0.6	0.6	0.3	0.3	0.3	0.3	0.3
Below line: Percentage point contributions to Q3 2024 3.1% real GDP								
First estimate for Q4 is Thursday, January 30								

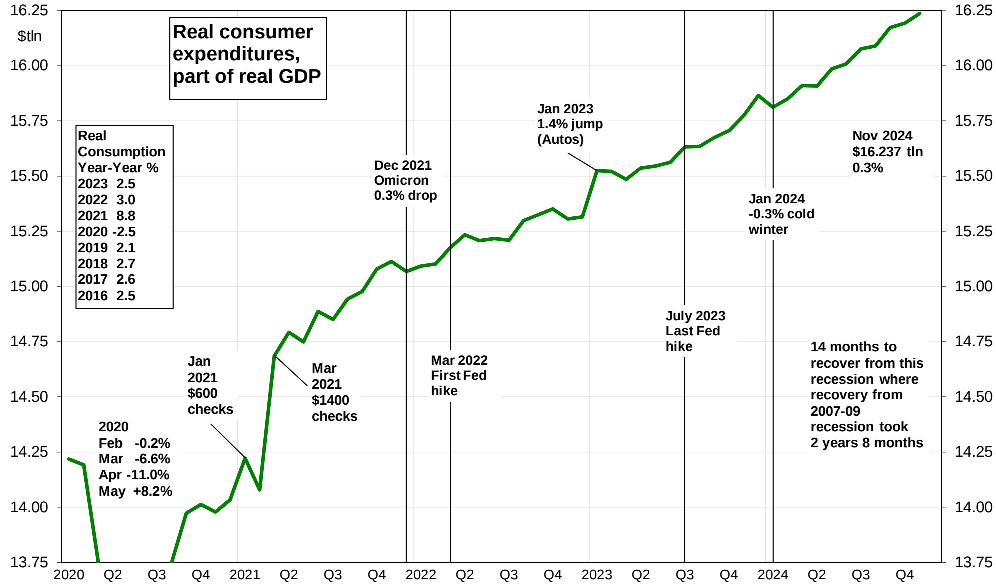
Other news at 830am ET was the unemployment insurance data. Weekly jobless claims fell back by 22K to 220K in the December 14 week, so no sign of immediate distress in the labor market.

Net, net, another false alarm of economic weakness as weekly job layoffs tumble back to earth this week and the last GDP figures under the Biden administration saw a solid upward adjustment to 3.1% in the third quarter from 2.8% reported previously. The incoming president-elect and his economic advisers will have to come up with something new to fix as the economy is already motoring along at the 3% speed limit. 3% steady growth was a goal in the first Trump administration and it is apparently the goal in the second Trump administration listening to the incoming Treasury secretary. Consumer spending, exports and business investment increased in the third quarter contributing to the upward revision. The consumer showed no concern about the upcoming elections with real consumption expenditures soaring 3.7% in the third quarter. Stay tuned. The economy looks picture perfect upon revision and the need to fire up growth by a new President and a new Congress seems unwise if not risky.



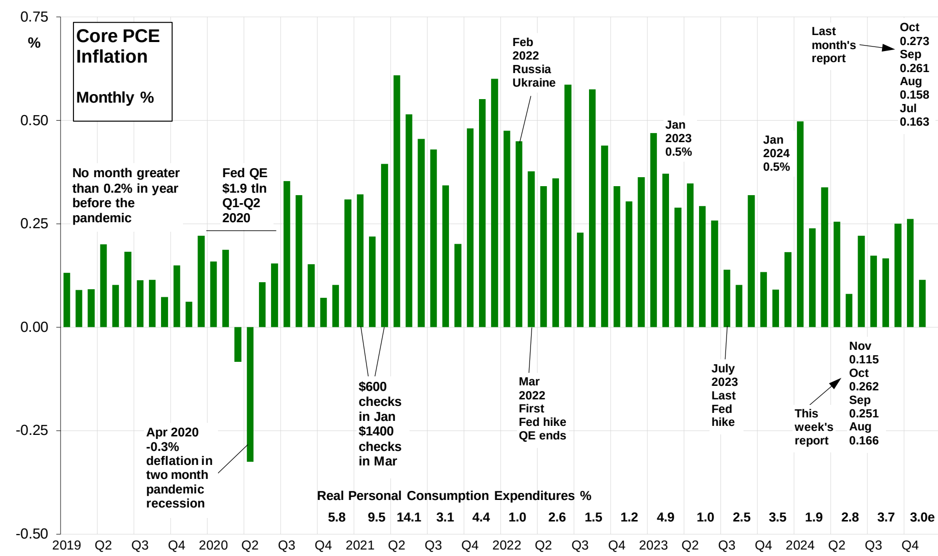
Spending solid, inflation feeble (Friday)

Breaking economy news. Personal income report for November. The market was pretty beat up this week, but somehow the core PCE inflation increase of 0.1% versus the 0.2% consensus estimate, lifted both bond and stock prices. Trading conditions are on the thin side. Powell said at the press conference last week that core PCE inflation would be 2.8% year-on-year which means more or less the monthly change had to be 0.1% to match the 0.1% increase in November 2023. Not for anything, but this is the time of year when upward price pressures are weak.



Real consumer spending rose a solid 0.3% in November thanks to auto sales in the durable goods category. We would not think consumers are buying in advance of potential tariffs, but you never know. Real consumer spending is supportive of a 3% real GDP number for the fourth quarter, to be released Thursday, January 30, 2025.

Net, net, economic growth is literally on a tear at the end of the year as consumers are buying boat loads of computers and new cars and SUVs. The election results cheered almost exactly half of the country and they flocked to the shops and malls. Wages and salaries were up 0.6% in November, the most looking back to April, which means consumer spending will finish the year with a bang. Consumers have the money and they are spending it. There was even some good news on the inflation front with core PCE prices rising just 0.1% in November even if the year-on-year rate remains stuck at 2.8% as Powell "forecast" at Wednesday's press conference. Whether core consumer prices continue to rise only 0.1% each month is an open question, but at least the weakest increase since May this year will be enough to prompt a couple of Fed rate cuts in 2025. Stay tuned. Consumer spending in the third quarter shot the lights out despite the election uncertainty with spending of 3.7% and now it is running a solid 2.7% in the fourth quarter with only December data left to report. If Washington can keep the tires from coming off the bus, the economy might just surprise us on the upside in 2025. Bet on it.



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