

# Morning Market Tidbits

## Rules are made to be broken

### In focus

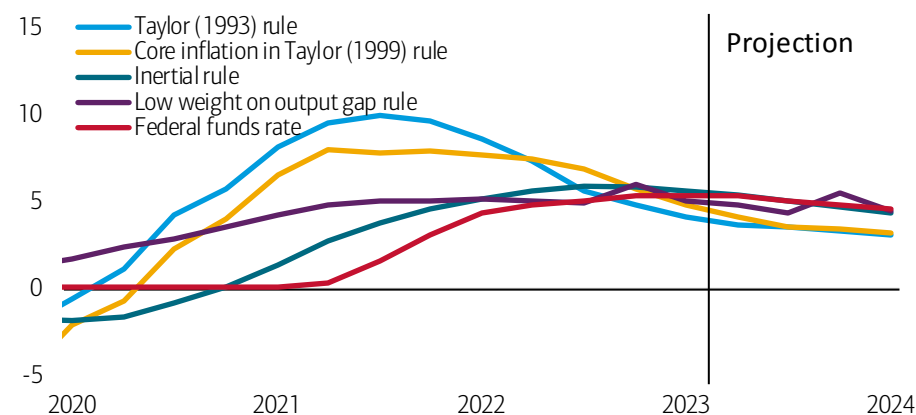
Last week, comments from Federal Reserve Governor Waller led rates to rally and the market to price in more cuts in 2024. Specifically, markets latched onto Waller's answer to a question about cuts: "There's certainly good economic arguments from any kind of standard Taylor rule that would tell you if we see this inflation continuing for several months .... You can then start lowering the policy rate just because inflation is lower."

Waller's answer did not surprise us. We have long argued that the Fed will cut rates gradually next year as inflation continues to move lower. Indeed, we expect the Fed to cut for the first time in June 2024 and then at a pace of 25bp/quarter thereafter. What was somewhat surprising, however, was the shift in Waller's tone, which has become more balanced, if not dovish, of late. We view Waller as a bellwether on the committee. Therefore, his recent remarks suggest that the Fed is moving from "hawkish holds" to "dovish holds."

In addition to the slight shift in tone, much was made of Waller's reference to the Taylor rule. Here we think that it was more a means to support his argument that cutting rates because inflation is low makes sense than a sign of any rules-based policy making. As we have learned over time, monetary policy rules do not dictate the path of policy, which is more discretionary. We only need to look back over the last few years to see that the Fed responded more slowly and less aggressively to inflation than policy rules would suggest (Exhibit 1). Like the current hiking cycle, we do not expect the Fed to follow a rules-based cutting cycle.

### Exhibit 1: Monetary policy rules versus the actual federal funds rate (%)

Policy rules were not followed to a tee during the latest hiking cycle



Source: BofA Global Research

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Timestamp: 07 December 2023 08:28AM EST

## Market action

The Asian equity markets that we cover closed negative overnight. Looking at individual markets, we note that the Nikkei, the Hang Seng, and the Indian Sensex fell 1.8%, 0.7%, and 0.2%, respectively, while the Shanghai Composite and the Korean Kospi were down 0.1% each.

As of 7:00 am ET, aggregate European stocks are down 0.2%, and S&P,500 futures are flat. In the bond markets, 10-year Treasury yields are 5bp higher at 4.15%, and German Bund yields are 2bp lower at 2.18%. The dollar index is down \$0.25 to \$103.90. West Texas Intermediate (WTI) crude oil prices are \$0.41 higher at \$69.79/barrel, and gold prices are at \$2032.65/ounce.

## Data review

### Trade Balance

The October trade deficit was in line with expectations at \$64.3B, widening slightly from the slightly revised up September deficit of \$61.2B. Imports rose 0.2% in October to \$323.05b from \$322.56b in September, and exports fell 1% to \$258.79b from \$261.41b previously. This is pretty much in line with the advance goods trade deficit print, where exports fell by 1.7% m/m, and imports came in flat. Imports remain stable as the US consumer continues on a resilient path on the back of still-tight labor market, low layoffs, and excess savings. Additionally, the services surplus increased from \$25.1b to \$25.5b, supported by net travel services, where visits by overseas residents to the US improved further as travel has more or less normalized. Also, the trade deficit excluding petroleum rose to \$67.5b in October from \$63.5b in September, and the real goods deficit widened slightly as well.

### Productivity and Labor Costs

Productivity was revised up by five tenths to 5.2% q/q saar (seasonally adjusted annual rate) in its final 3Q print on the back of the rise in 3Q GDP in the second estimate to 5.2% from 4.9% previously. Meanwhile, unit labor costs were revised down from -0.8% to -1.2%. Compared to a year ago, productivity is up 2.4% after a period of weakness in 2022.

## Data preview

### Data in the week ahead

December 7

Date	Time	Indicator	Period	BofA	Consensus	Previous
				Estimate		
12/07/23	8:30	Initial Jobless Claims	Dec 02	222k	—	218k
12/07/23	10:00	Wholesale Inventories	Oct F	—	—	-0.2%
12/07/23	15:00	Consumer Credit	Oct	—	\$9.0b	\$9.1b

Source: Bloomberg, BofA Global Research

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### Initial jobless claims

Initial jobless claims are likely to increase to 222 thousand (k) in the week ending December 2 after the 7k rise to 218k in the previous week. Last week's Thanksgiving period rise paid back some of the 22k decline in the week ending November 18. Claims are a volatile measure, even more so around the holidays. But the four-week moving average remains almost unchanged at 220k. The low level of claims these past weeks has highlighted a moderating labor market characterized by low layoffs and slow hiring. In addition to some impact of seasonal factors, the rise in continuing claims, which should continue, is also consistent with a slowdown in the hiring rate and hence people finding it more difficult to secure employment.



## US GDP Tracking

### Exhibit 2: BofA US GDP tracking estimate (% q/q saar)

Our 4Q GDP tracking estimate is down three-tenths to 1.0% q/q saar largely due to weaker-than-expected wholesale and retail inventories in October and larger-than-expected widening in the advance goods trade deficit in October

Date	Data release	GDP	Final Sales	PCE	Res. Inv.	Struct	Equip	IPP	Gov.	Exports	Imports	(level)	(level)
11/21/23	Existing Home Sales	<b>1.4</b>	1.8	1.8	<b>-0.6</b>	-0.8	2.6	2.5	2.0	8.1	5.5	-936.1	45.3
11/22/23	Durable Goods Orders	<b>1.3</b>	<b>1.7</b>	1.8	-0.6	-0.8	<b>1.3</b>	2.5	2.0	8.1	5.5	-936.1	<b>40.2</b>
11/27/23	New Home Sales	1.3	1.7	1.8	<b>-2.2</b>	-0.8	1.3	2.5	2.0	8.1	5.5	-936.1	40.2
11/30/23	3Q GDP (S), Advance Goods Trade Balance, PCE	<b>1.0</b>	<b>1.8</b>	<b>2.0</b>	-2.2	-0.8	1.3	2.5	2.0	<b>8.4</b>	<b>6.4</b>	<b>-938.2</b>	<b>26.0</b>
	GDP tracking	1.0	1.8	2.0	-2.2	-0.8	1.3	2.5	2.0	8.4	6.4	-938.2	26.0
	Contribution to GDP growth (pp)			1.3	-0.1	0.0	0.1	0.1	0.3			0.0	-0.8
	BofA official GDP forecast	1.5	2.0	2.0	1.0	1.0	2.0	2.5	2.0	3.0	2.0	-936.0	40.5

**Source:** BofA Global Research. Our GDP tracking estimate reflects the mechanical aggregation of incoming data that directly informs the BEA's GDP calculations. The process is distinct from our official published GDP forecast. Boldface cells indicate where data have implications for tracking estimates.

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## Overseas data

### Germany

October industrial production slowed to -0.4% on the month, below market expectations of a 0.2% increase. Our Europe economists note that compared to the downside to the factory orders data earlier this week, this is a smaller surprise – demand can weaken, and output in the sector can remain relatively more resilient for a while, given the still very high level of backlogs of orders.

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