J.P.Morgan

US Rates Strategy post-election update

Fixed Income Strategy

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Governments *J. Barry, P. White, A. Borges, L. Wash*
Treasury yields remain near their highest levels since early-July, OIS forwards are pricing in a less dovish path for Fed policy than our revised forecast, and intermediate Treasuries have not diverged this sharply from their drivers since last fall's term premium scare. This backdrop presents a favorable location for adding duration, but the momentum to higher yields remains strong and our Treasury Client Survey sits near its longest levels of the year. We remain neutral on duration, but recommend holding 50:50 weighted 2s/7s/30s belly-richening butterflies as a low-beta way to position for lower yields. Stronger CPI or retail sales pose a risk to this trade, and we would use further outperformance to reduce risk. We discuss risks to Treasury supply and the debt ceiling stemming from a red sweep. Despite the uncertainty around the sequence and timing of policy action under the new administration, breakevens appear to incorporate little premium for the risk of a supply shock coming from more hawkish immigration policies or higher tariffs. We think there is room for TIPS breakevens to continue wider and recommend holding 5-year breakeven wideners on a nominal beta-weighted basis.

Interest Rate Derivatives *S. Ramaswamy, I. Ozil, P. Michaelides, A. Parikh*
Swap spreads widened, likely in anticipation of de-regulatory tailwinds, but this is both exaggerated and premature - given upside risks to UST duration supply, we recommend re-entering swap spread narrowers and spread curve flatteners. We update our Fed balance sheet forecast, and now expect QT to end in March. Implied volatility has declined in excess of expectations given the passing of event risk, but delivered volatility should remain elevated - stay bullish on gamma.

Short-Term Fixed Income *T. Ho, P. Vohra*
A higher terminal rate should position MMFs as an attractive liquidity investment compared to other cash options, keeping AUMs high. With no end to QT mentioned at the November FOMC meeting, declining ON RRP balances, and expectations of a less contentious debt ceiling debate and less protracted TGA drawdown, we've moved our QT end prediction to 1Q25.

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See page 37 for analyst certification and important disclosures.

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Treasuries

Fading event risk and cheap valuations are supportive: maintain 2s/7s/30s belly-richening butterflies

- Yields traded a wide range this week, with the Treasury curve bearishly steepening as a red sweep came into view, but reversing most of these moves amid a modestly dovish FOMC outcome on Thursday
- Yields now sit at their highest levels since early-July and closely reflect the high probability of a red sweep in online election markets. OIS forwards are pricing in a less dovish path for Fed policy than our revised forecast, and intermediate Treasuries have not diverged this sharply from their drivers since last fall's term premium scare
- This backdrop presents a favorable location for adding duration, but the momentum to higher yields remains strong and our Treasury Client Survey sits near its longest levels of the year, so we stay neutral on duration
- However, the belly had sharply underperformed: we recommended adding 50:50 weighted 2s/7s/30s belly-richening butterflies as a low-beta way to position for lower yields. Stronger CPI or retail sales pose a risk to this trade
- Though a red sweep should not impact the budget deficit before FY26, given the large funding gap we identified between FY26-FY29, there is a risk Treasury may need to begin raising coupon auction sizes earlier than our November 2025 forecast
- We think the upcoming expiry of debt ceiling legislation should not provide a repeat of 2011, 2013, 2015 or 2023 episodes, as the most contentious debates have come with a Democrat in the White House and Republican control of the House. Nevertheless, with the expected "x date" likely to fall in July and the Trump administration occupied with cabinet confirmations, trade, and immigration policy in early-2025, we do not expect resolution before early 2Q25

Market views

In a week ripe with event risk, Treasury yields traversed a wide range, with 10-year yields hitting a local low of around 4.25% on Monday, only to retrace higher toward 4.50% in reaction to the results of the US presidential election. Indeed, long-end yields rose 15bp and the curve bearishly steepened Tuesday evening into Wednesday amid the Republican party's strong performance . The latest polls had suggested this to be the closest presidential election in modern history, but instead former President Trump has won the presidency with a strong electoral college majority, as well as a popular vote majority. This had strong implications for the Congressional races as well, as Republicans appear set to take a larger majority in the Senate than anticipated, and online prediction markets indicate a high probability that they will maintain a small majority in the House as well. However Treasuries unwound more than half of those move on Thursday, amid a somewhat more dovish outcome at the FOMC meeting (**Figure 1**).

As expected, the FOMC lowered the Fed funds range by 25bp to 4.5-4.75%. The statement saw small changes: unlike in September, there was no hawkish dissent. Perhaps the most interesting part of the press conference was when Chair Powell was asked if "the President has the power to fire or demote you and has the Fed determined the legality of a President demoting at will any of the other governors with leadership positions?" Powell firmly defended the Federal Reserve Act and the independence of the institution, responding "Not

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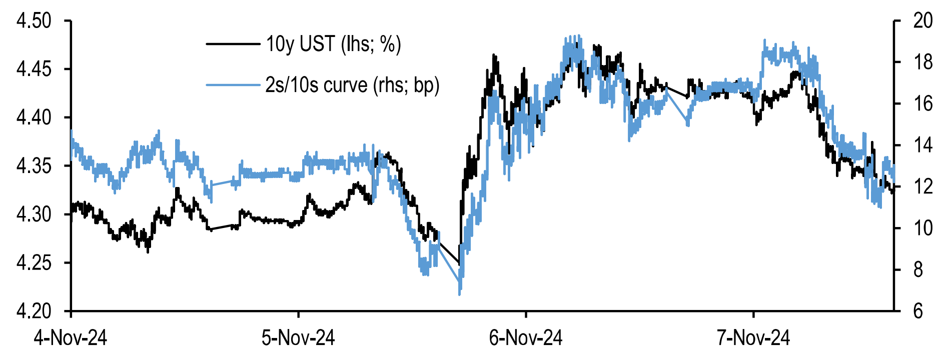
permitted under the law" (see *He's not leaving*, Michael Feroli, 11/7/24). In the week-to-date, 2-year yields have risen 2bp, while 5-, 10-, and 30-year yields have each declined 2bp.

Figure 1: The curve steepened bearishly as the election results indicated a red sweep was likely but retraced most of these moves later in the week

10-year Treasury yields (%, lhs) versus 2s/10s Treasury curve (bp; rhs)



Source: J.P. Morgan

As we look ahead, we think the old Brainard attenuation principle holds, and that the various policy uncertainties stemming from the election outcome may lead the Fed to move more slowly than it otherwise would: while we continue to project a 25bp ease at the December FOMC meeting, we now forecast the Fed will ease at a quarterly pace next year, and to a terminal rate of 3.5% in 2026 (versus our prior forecast of cutting each meeting until the Fed funds rate reaches 3% in 2H25, see *Economic implications of the elections*, Michael Feroli, 11/6/24).

As a result, the change to the Fed forecast and the election outcome require a change to our interest rate forecast. Clearly, a Fed that eases more slowly and to a higher terminal rate should translate to Treasury yields which remain more elevated than we had previously expected, and also flatter yield curves versus our prior forecasts. Moreover, the election results should also lead to more anchored Treasury yields for three distinct reasons.

First, as we've discussed in the past, President Trump's previous term was marked by an unorthodox style of addressing trade and monetary policy via social media posts, and this communication style played a statistically significant role in elevating implied volatility (see *Introducing the Volfefe Index: Quantifying the impact of presidential tweets on rates volatility*, 9/6/19). Should he proceed similarly in a second term, elevated volatility could also contribute to higher term premium, as we have found volatility is a key driver in academic measures of term premium (see *In the eye of the beholder*, 9/12/23). **Second**, a red sweep raises the likelihood of fiscal expansion versus prior baseline forecasts, which likely anchors growth and inflation expectations at higher levels than our prior forecast. **Third**, as a result, the Treasury market will continue to grow more rapidly than demand from its traditional dominant set of price insensitive investors, namely the Fed, foreign investors, and US banks, that comprised as much as a 70% share of Treasury market ownership in the middle of the last decade. The expected shift in demand should further elevate term premium.

Given these factors we present our updated interest rate forecast in **Figure 2**. **Given the less dovish Fed forecast, we raise our YE24 2-year forecast from 3.85% to 4.25%, and our 2Q25 forecast from 3.20% to 3.80%). We also raise our YE 10-year target from 3.90% to 4.50% and our 2Q25 forecast from 3.40% to 4.15% to reflect the dynamics discussed above.**

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Figure 2: We raise our interest rate forecasts higher to reflect a shallower path of Fed easing to a higher terminal rate, as well as higher inflation expectations and term premium following the US election outcome

J.P. Morgan US interest rate forecast; %

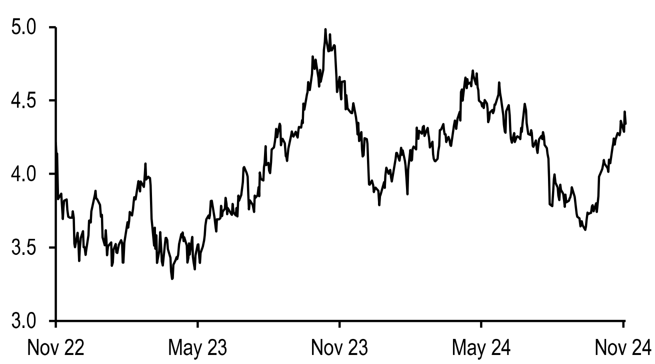
	Actual	1m ahead	4Q24	1Q25	2Q25	3Q25
	7-Nov-24	7-Dec-24	31-Dec-24	31-Mar-25	30-Jun-25	30-Sep-25
Rates (%)						
Effective funds rate	4.83	4.58	4.35	4.10	3.85	3.60
SOFR	4.81	4.56	4.40	4.15	3.90	3.65
2-yr Treasury	4.22	4.20	4.25	4.00	3.80	3.65
3-yr Treasury	4.18	4.15	4.20	4.00	3.80	3.65
5-yr Treasury	4.19	4.20	4.25	4.05	3.90	3.80
7-yr Treasury	4.26	4.25	4.35	4.15	4.00	3.90
10-yr Treasury	4.34	4.35	4.50	4.35	4.15	4.10
20-yr Treasury	4.64	4.65	4.80	4.65	4.45	4.40
30-yr Treasury	4.54	4.55	4.75	4.65	4.45	4.50
Spreads (bp)						
Fed funds/2yr	-61	-38	-10	-10	-5	5
2s/10s	12	15	25	35	35	45
2s/5s	-3	0	0	5	10	15
5s/10s	15	15	25	30	25	30
5s/30s	35	35	50	60	55	70
10s/30s	20	20	25	30	30	40

Source: J.P. Morgan

Against this backdrop, yields remain near their highest levels since the beginning of the summer, at levels which have only been briefly seen over the last two years (**Figure 3**) . To an extent this has been supported by a less dovish path for expected Fed policy over the next year, as OIS forwards are now pricing 17bp of easing over the balance of 2024, 68bp in 2025, and a trough closer to 3.60% (**Figure 4**). Indeed, to the extent that money markets are pricing in a more dovish path for Fed policy than our own forecasts, this would indicate that Treasury yields should find some more stability in the coming weeks, particularly as the prospects for trade policy and immigration reform are not yet known.

Figure 3: Treasury yields have retraced to their highest levels since early-July...

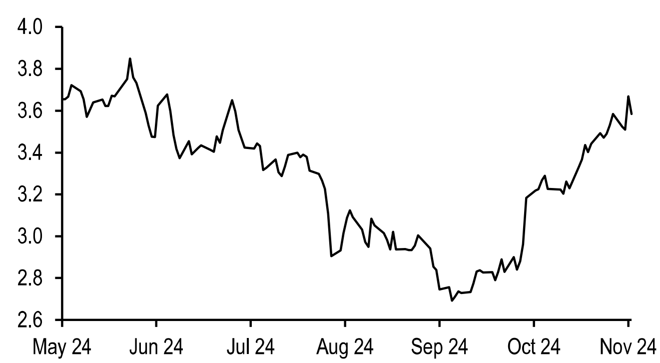
10-year Treasury yields; %



Source: J.P. Morgan.

Figure 4: ...as markets are pricing in a significantly shallower pace of Fed cuts in the coming years...

OIS forward-implied trough in Fed funds rate; %



Source: J.P. Morgan

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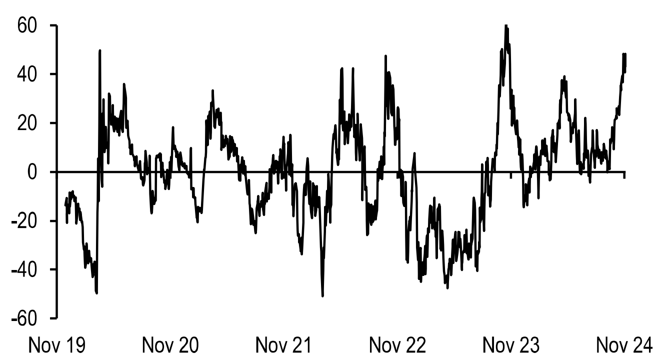
Similarly, our valuation framework would indicate there is some value as well: 10-year yields are trading about 40bp too high after controlling for the market's Fed policy, inflation, and growth expectations, a gap of more than 2 standard deviations (**Figure 5**). Treasuries last diverged this significantly from their underlying drivers in fall 2023, when Fed guidance indicated risks of more policy tightening, and Treasury was in the early stages of large, open-ended increases to long-duration auction sizes. Before that, in the fall of 2022, a similar-sized gap opened following the UK mini budget crisis, in which Treasury yields were dragged higher amid the deleveraging in the Gilt market. In both of these instances, yields ultimately ended up declining to converge with their fundamental drivers. However, we recognize that the scope for a full reversal may be limited, as the reaction in most asset classes since the election results is indicative of stronger growth and inflation outcomes in the future. **Indeed, while we have argued that increased use of tariffs is likely to be a tax on consumers and negatively impact business sentiment, weighing on growth, with inflation still sitting above the Fed's 2% target, we are respectful that markets view this as inflationary, which is likely to keep yields anchored at higher levels.** Moreover, our latest *Treasury Client Survey*, taken *before* the election, moved to its longest levels since mid-August, when weakening labor markets were at the forefront of market concerns, and near the longest levels of the past year (**Figure 6**).

Figure 5: ...and Treasuries are now cheaper relative to their underlying drivers than at any point since last fall

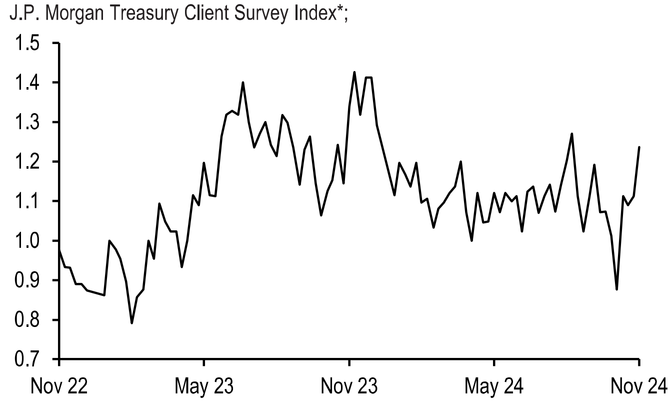
J.P. Morgan 10-year Treasury yield fair value model residual*; bp



*10-year Treasury yields regressed on 3m3m OIS rates (%), 5y5y seasonally-adjusted TIPS breakevens (%), J.P. Morgan U.S. Forecast Revision Index (%), Fed forward guidance (months), and SOMA share of outstanding marketable US Treasury debt, excluding T-bills (%). Regression over the last 5 years: R-squared = 97.8%, SE = 20.2bp
Source: J.P. Morgan, US Treasury, Federal Reserve Bank of New York

Figure 6: Our client survey indicated clients had added duration ahead of the election

J.P. Morgan Treasury Client Survey Index*;



* (Longs+Neutrals)/(Shorts+Neutrals)
Source: J.P. Morgan

Nevertheless, we don't want to miss the forest for the proverbial trees: with Treasuries realizing most of the move we would expect from a red sweep, money markets pricing in slightly less easing than our modal view, and valuations cheap, there is more value in Treasuries than we have seen in some time. Along the curve, we think the belly looks extremely attractive: the 7-year sector had underperformed the broad curve by 15bp at its peak, and had appeared 6bp cheap after controlling for the level of 7-year yields and the slope of the 2s/30s curve (**Figure 7**). Moreover, positioning for 7-year sector outperformance trades like a low-beta duration long and broad curve flattener, and we are comfortable taking this risk in the context of the factors mentioned above. **Accordingly, we recommended 50:50 weighted 2s/7s/30s Treasury butterflies as a lower-beta way of positioning for lower yields** (see *US Treasury Market Daily*, 11/6/24).

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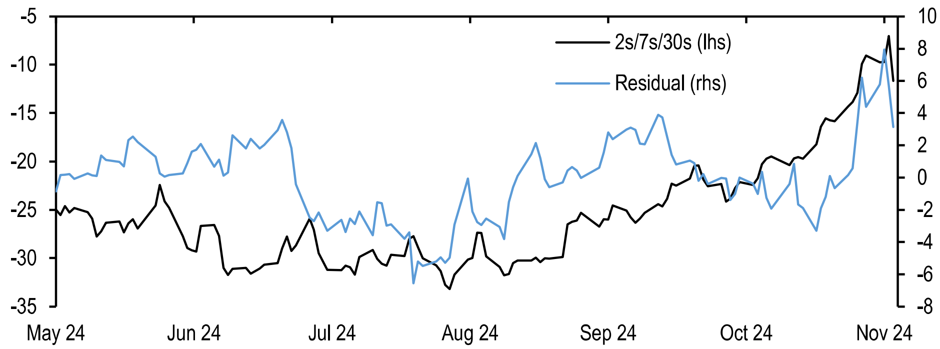
Figure 7: The 7-year sector has underperformed more than would be implied by the rise in yields in recent weeks

50:50 weighted 2s/7s/30s Treasury butterfly (lhs, bp) versus residual of 50:50 2s/7s/30s butterfly regressed on 7-year Treasury yields and 2s/30s Treasury curve* (rhs; bp)



* 2s/7s/30s = (19.70*5-year UST yields) + (0.2695* 2s/30s curve) -107.621. R-squared = 79.7%, SE = 2.5bp
Source: J.P. Morgan

Given how this trade has moved over the last day, we would use further belly outperformance to pare back this soft long exposure, as there is significant event risk over the near term. Next week brings the October CPI and retail sales reports: consensus projects a 0.3% rise in core CPI for the second consecutive month, and we think there is potential for a strengthening in core relative to recent months, given the signals coming from industry data on used cars and airfares (see *TIPS*). Separately, our Quant Econ Dashboard implies control retail sales rose 0.6% in October, stronger than the 0.2% consensus (see *Quant Econ Dashboard*, 11/7/24). Upside risks to both of these data points may dampen the implied probability of a December ease, and hence result in higher Treasury yields.

Treasury supply and the debt ceiling in 2025

Turning to Treasury supply, we have argued in recent weeks that a Republican sweep is the most bearish outcome for the long end of the curve, given the rapid growth of the Treasury market means ownership is shifting from price insensitive investors like the Fed, foreign official institutions and US banks toward more price sensitive investors, (see Treasuries, *U.S. Fixed Income Markets Weekly*, 10/18/24). Indeed, according to bipartisan research from the Committee for a Responsible Federal Budget President Trump's plan would increase the federal debt by $7.5tn during the 2026-2035 period. We had previously assumed that given the borrowing capacity created over 2H23-1H24, Treasury could keep coupon auction sizes unchanged until November 2025, but this result could move that timeline forward (see *Wait till next year*, 5/24/24). Importantly, individual income tax cuts from the 2017 TCJA don't expire before the end of 2025, so the bulk of the widening in financing needs relative to prior expectations should materialize from FY26 onward. Overall, **a Republican sweep should widen Treasury's financing gap, and will therefore necessitate larger coupon auction sizes over time than previously expected, and there's a risk those increases will take place earlier than expected, potentially in August or even May of next year.**

Away from the near-term implications, we would also note **the election outcome reduces the risks of a contested debt ceiling debate and uncertainty around the evolution of the TGA in 1H25**. As a reminder, the debt limit has been suspended through January 1, 2025 and following this date, Treasury will begin utilizing extraordinary measures and the funds in its general account to meet its obligations. Assuming Treasury's $700bn TGA forecast for 4Q24, and a slight increase in extraordinary measures compared with the last debate in 2023, we think it's unlikely Treasury will exhaust all these resources and risk a technical

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default before July 2025. We continue to think the TGA should be biased lower in 1Q25 – even in a relatively friendly debt ceiling resolution, the Trump administration will have to nominate cabinet appointments and have them approved, and we think trade and immigration policy will take on a greater priority before the debt ceiling is debated (see *US Treasury Market Daily*, 10/28/24).

Moreover, we think this election result portends for a less contentious debate. Historically, the most contested debt ceiling debates have taken place under a Democratic President and a Republican-controlled House, like in 2011, 2013, 2015, and 2023. Though there is some uncertainty over which party will control the House, we expect the passage of new debt ceiling legislation well in advance of the "x date" in either scenario. Looking at recent debt ceiling episodes, we think the 2025 backdrop has the most in common with 2017 and 2019, and between the two, 2017 strikes us as the best analogue. As a reminder, while it took Congress nearly six months to act, the debt limit was ultimately suspended on September 8, well in advance of the forecasted October "x date", so this was relatively timely. Tentatively, we have penciled in that the TGA would finish 1Q25 at $550bn, which still appears appropriate. Additionally, we think it's fair to assume a debt ceiling resolution by early 2Q25, which would allow Treasury to bring the TGA back up to more normal levels by the middle of the year.

The election and regulatory reform

The election outcome also raises the likelihood of a material shift in the regulatory environment stemming from changes in Fed's supervision. Notably, Governor Tarullo, who was de factor Vice Chair for supervision during the Obama administration, tendered his resignation in February 2017 following the handoff to the first Trump administration. Similarly, his successor, Governor Quarles, stepped down soon after the expiration of his 4-year Vice Chair term in October 2021 following a similar handoff from Trump to Biden earlier that year, despite more than a decade left in his governorship term. If Vice Chair for Supervision Barr — whose Vice Chair term expires in July 2026 — follows in his predecessor's footsteps, there is scope for the Trump administration to move quickly in appointing a new Vice Chair for Supervision once Barr's tenure ends in 2026. As the confirmation process for Fed Vice Chair only has to pass the Senate and given the current evolving Congressional landscape, it might be easier to confirm a new Vice Chair for Supervision.

The potential change in Fed regulatory leadership comes at a time when policy makers and market participants alike are increasing their focus on reduced intermediation capacity in the Treasury market and exploring ways to expand dealer capacity. Panelists at the recent Treasury market conference highlighted the role of regulatory burdens, most notably the enhanced Supplementary Leverage Ratio (eSLR), in preventing dealers from both growing their balance sheets alongside the growth in the Treasury market and increasing the flexibility of their balance sheets. It was noted that temporary SLR relief in 2020-2021 resulted in increased dealer intermediation of Treasuries (see *Time flies: Reviewing the tenth annual Treasury market conference*, 9/26/24). Against this backdrop it is notable that at the November refunding, TBAC presenter suggested a number of policy changes to improve market functioning, including an exemption of central bank reserves and Treasuries from the SLR, either on a countercyclical temporary basis or permanently as part of a holistic update to capital regulation (see *US Treasury Market Daily: November refunding review*, 10/30/24).

While it is uncertain who could take the regulatory helm at the Fed, Governor Bowman, a Republican nominated by Trump to the community banking seat at the Board, is well positioned for the next Vice Chair for Supervision role. In a speech this summer Bowman lamented the "missed opportunities in capital reform" from the "current narrow approach to rulemaking", noting that "Treasury market intermediation can be disrupted by constraints imposed by the eSLR…[and] it seems prudent to address this known leverage rule constraint before future stresses emerge that would likely disrupt market functioning." This stands in contrast to Vice Chair Barr's most recent comments made at the Treasury market conference in September [1] While SLR relief would represent a net positive for Treasury market liquidity, it would likely be a slow process, if taken up at all, since the Fed would also need cooperation from the FDIC and the OCC as well.

Trade recommendations

- **Initiated 50:50 weighted 2s/7s/30s belly-richening butterflies**

- Sold 50% risk, or $66mn notional of T 4.125% Oct-26s (yield: 4.266%; bpv: $188/mn)
- Bought 100% risk, or $41.9mn notional of T 4.125% Oct-31s (yield: 4.359%; bpv: $591/mn)
- Sold 50% risk, or $7.7mn notional of T 4.5% Nov-54s (yield: 4.598%; bpv: $1600/mn)
- (*US Treasury Market Daily*, 10/6/24: P/L since inception: +4.4bp)

- **Maintain 91:100 weighted 3.125% Nov-41/ 2% Nov-41 flatteners**

- Stay short 91% risk, or $20mn notional of T 3.125% Nov-41s
- Stay long 100% risk, or $24.7mn notional of T 2% Nov-41s
- (*US Fixed Income Markets Weekly*, 9/20/24: P/L since inception: -2.9bp)

- **Unwound 75%/6% weighted 5s/10s/30s belly-cheapening butterflies**

- Stay long 75% risk, or $43mn notional of T 4.625% Sep-28s
- Stay short 100% risk, or $33.3mn notional of T 3.875% Aug-33s
- Stay long 6% risk, or $1mn notional of T 4.125% Aug-53s
- (*US Fixed Income Markets Weekly*, 9/29/23: unwound in *US Treasury Market Daily* on 11/6/24 with 8.5bp P/L)

- **Maintain 23:84 weighted 2s/7s/10s belly-richening butterflies**

- Stay short 23% risk, or $28mn notional of T 4.375% Jul-26s
- Stay long 100% risk, or $40.2mn notional of T 4.125% Jul-31s
- Stay short 84% risk, or $23mn notional of T 3.875% Aug-34s
- (*US Treasury Market Daily*, 8/21/24: P/L since inception: -4.0bp)

1. *Liquidity, Supervision, and Regulatory Reform*, Michelle Bowman, 7/18/24

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Figure 8: Closed trades in last 12 months

P/L reported in bp of yield unless otherwise indicated

TRADE	ENTRY	EXIT	P/L
Duration			
7-year duration shorts	11/03/23	11/22/23	-7.9
30-year duration shorts	12/15/23	01/04/24	10.9
5-year duration longs	01/19/24	02/01/24	25.3
5-year duration longs	02/09/24	03/07/24	3.3
Equi-notional 2s/5s flatteners	05/31/24	06/06/24	16.0
5-year duration shorts	06/14/24	07/01/24	21.9
30% 2-year duration short	07/12/24	07/31/24	-1.8
Curve			
10s/30s steepener	11/03/23	11/22/23	-7.3
2s/5s flatteners	12/08/24	05/17/24	6.0
5s/30s steepener	11/22/23	09/06/24	26.4
3s/5s steepener	09/04/24	09/06/24	3.1
3s/30s steepener	09/06/24	09/18/24	0.2
3s/20s steepener	09/27/24	10/04/24	-18.3
Relative value			
2.75% Aug-32/ 3.5% Feb-39 steepeners	01/10/24	01/26/24	5.2
20s/ old 30s flatteners	02/15/24	05/10/24	-2.6
100:97 weighted 3.75% Apr-26/ 4.625% Sep-26 flatteners	04/12/24	05/17/24	2.2
100:95 weighted 4% Feb-28 / 4% Feb-30 steepeners	02/23/24	05/31/24	-6.6
50:50 weighted 3s/5s/7s belly-richening buterflies	03/15/24	06/14/24	2.1
100:98 weighted 4.75% Feb 37s / 4.5% Aug 39s steepeners	06/14/24	07/12/24	2.6
100:95 weighted 0.625% Jul-26s / 1.25% Dec-26s steepeners	07/12/24	08/14/24	1.5
Term premium			
75:6 weighted 5s/10s/30s belly-cheapening butterfly	09/29/23	11/06/24	8.5
Number of positive trades			15
Number of negative trades			6
Hit rate			71%
Aggregate P/L			90.7

Source: J.P. Morgan

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TIPS Strategy

Clarity on election outcome, but policy uncertainty remains

- Breakevens widened sharply in the aftermath of the election results, but gave up some of these gains on Thursday alongside a retracement lower in nominal yields
- Though we have clarity on the outcome of the presidential election, and near-certainty that both chambers of Congress will be in Republican control, there remains considerable uncertainty around the sequence, timing, and magnitude of policy action under the new administration...
- ...our baseline assumptions reflect a relatively small impact of policy changes on inflation in 2025, although we recognize that risks are skewed to the upside, which should keep TIPS supported over coming months
- Next week focus shifts to the October CPI report, which has the potential to show strengthening versus recent months. Any upside surprise in core CPI, against a backdrop of still-elevated political uncertainty, could help to amplify demand for inflation protection heading into 2025
- We continue to hold beta-weighted 5-year breakeven wideners paired with an energy hedge

Market views

Breakevens widened sharply in the aftermath of the election results, but gave up some of these gains on Thursday alongside a retracement lower in nominal yields. On net, 5-, 10-, and 30-year breakevens are 5bp, 3bp, and 1bp wider WTD, although more granularly, outperformance was largely concentrated at the very front end: 2-year inflation swaps rose 16bp and 1Yx1Y inflation swaps rose 13bp to 2.71%, sitting near their highest level since December 2022 (**Figure 9** & **Figure 10**). The real yield curve bull steepened, with 5-year real yields 7bp lower. Oil prices traded in a narrow range, ending roughly 3% higher WTD. Thursday's FOMC meeting clearly took a backseat to political developments, but Chair Powell's commentary at the post-meeting press conference were marginally dovish, highlighting that ex-housing core PCE inflation is basically back at levels consistent with target inflation, labor markets are not a source of inflationary pressure, and inflation expectations are consistent with 2% inflation. We think this guidance is consistent with another 25bp cut in December, though we expect the Fed can slow to a quarterly pace of cuts beginning in the first quarter of next year (see *He's not leaving*, Michael Feroli, 11/7/24).

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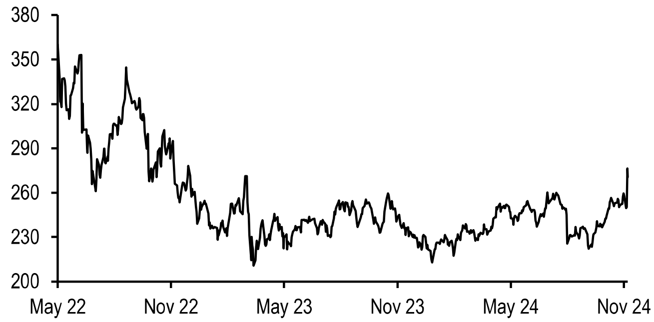
Figure 9: 1Yx1Y inflation swaps jumped 13bp MTD, to their highest levels since Dec 2022...

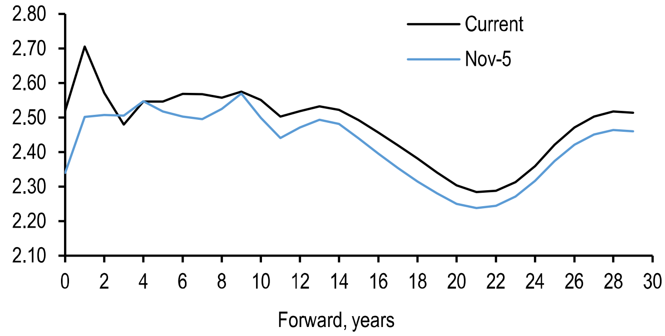
1Yx1Y inflation swap rate; %



Source: J.P. Morgan

Figure 10: ...outperforming sharply along the curve

Forward 1-year CPI inflation swap rates; %



Source: J.P. Morgan

As we look ahead, though we have clarity on the outcome of the presidential election, and near-certainty that both chambers of Congress will be in Republican control, there remains considerable uncertainty around the sequence, timing, and magnitude of policy action under the new administration. As a baseline, it is reasonable to assume that China will face significantly higher effective tariffs, while we recognize that the legal basis for implementing a 10% universal tariff is less straightforward. If tariffs are placed on China alone, the impact on consumer prices is likely to be less significant than if tariffs are done universally with every country, given the potential for trade to be diverted away from China, as was largely the case in the 2018-2019 episode. Additionally, Trump is also likely to move quickly on immigration policy, immediately ending the Biden-era asylum programs and taking other executive actions to suspend or ban certain types of immigration, although we recognize that the near-term impact on inflation is somewhat ambiguous (see *Economic implications of the election*, Michael Feroli, 11/6/24). **However, we still believe that inflation risks around this baseline are skewed to the upside, which should keep TIPS breakevens supported in coming months.**

Meanwhile, even with seasonally-adjusted breakevens trading near their widest levels of the last two years, it's notable that 2025 fixings continue to suggest a relatively subdued pace of core CPI inflation near 0.20%/month for most of next year (**Figure 11**). Additionally, the recent outperformance of TIPS represents a reversal of the sharp underperformance observed prior to election day, and seasonally-adjusted 5-year breakevens appear in line with the market-implied near-term path of Fed policy and broad commodity prices, incorporating little premium for the risk of a supply shock coming from more hawkish immigration policies or a ratcheting up of tariffs (**Figure 12**). Over the near term, market focus will turn to CPI next week. The market fixing is trading at 315.65, implying a 0.26% increase in headline and roughly a 0.30% increase in core CPI. Meanwhile, we recognize there is potential for a strengthening in core relative to recent months, given the signals coming from industry data related to more volatile categories such as used cars and airfares. Any upside surprise in core CPI next week, against a backdrop of upside inflation risk stemming from still-elevated political uncertainty, could help amplify demand for inflation protection heading into 2025. **Thus, we continue to hold 5-year beta-weighted breakeven wideners paired with a short energy hedge** (see *TIPS Strategy*, 11/18/24).

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Figure 11: The fixings curve suggests inflation expectations in 2025 moved higher but remains underpriced for tariff risk in our view

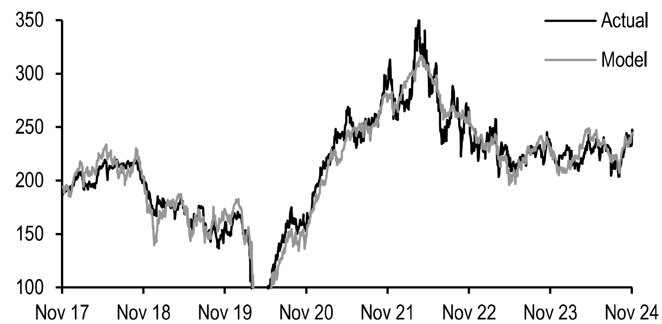
CPI fixings and implied inflation rates*; units as indicated

Month	Fixing	Implied headline m/m nsa	Implied headline % m/m sa	Implied headline % oya	Implied core % m/m sa	Implied core % oya
Oct-24	315.65	0.11%	0.26%	2.59%	0.30%	3.32%
Nov-24	315.44	-0.07%	0.30%	2.73%	0.35%	3.36%
Dec-24	315.48	0.01%	0.35%	2.85%	0.28%	3.36%
Jan-25	316.67	0.37%	0.14%	2.67%	0.14%	3.10%
Feb-25	317.73	0.34%	0.16%	2.39%	0.15%	2.89%
Mar-25	319.23	0.47%	0.20%	2.21%	0.24%	2.77%
Apr-25	320.12	0.28%	0.20%	2.10%	0.16%	2.63%
May-25	320.93	0.25%	0.09%	2.19%	0.16%	2.63%
Jun-25	321.79	0.27%	0.18%	2.42%	0.15%	2.72%
Jul-25	322.18	0.12%	0.16%	2.43%	0.16%	2.71%
Aug-25	322.73	0.17%	0.28%	2.52%	0.32%	2.75%
Sep-25	323.24	0.16%	0.18%	2.52%	0.22%	2.66%

* To derive market-implied core inflation rates, J.P. Morgan forecasts for food and energy CPI are used
Source: BLS, J.P. Morgan

Figure 12: The recent outperformance of TIPS on a cross-market basis reverses the underperformance observed just prior to election day, and breakevens remain close to our fair value estimates

J.P. Morgan 5-year breakeven fair value model estimate versus actual value*; bp



* 1m-forward, seasonally-adjusted breakevens are regressed on the J.P. Morgan Commodity Curve Index (JPMCCI) as well as its square and the 3mx3m/15mx3m OIS curve; regression over the last 7years; R2=93%, SE=9bp
Source: J.P. Morgan

Beyond the near term, we also revise higher our breakeven targets by 5-10bp across the curve over coming quarters, recognizing that a Red sweep should anchor both growth and inflation expectations at higher levels over the medium term. **Figure 13** shows that we now forecast 10-year breakevens at 235bp at the end of this year (versus 230bp previously). This forecast still reflects a narrowing in breakevens after 1Q25, primarily driven by a projected decline in energy prices. We still see risks to this breakeven forecast as skewed to the upside, for the reasons discussed above. Moreover, alongside changes to our Treasury yield forecasts, we now target 10-year real yields near 2.15% at year-end, followed by a more gradual decline in real yields over 2025.

Figure 13: We revise up our breakeven targets by 5-10bp across the curve, given the election outcome

Spot breakevens and real yields, breakeven targets, and real yield and curve levelsbasedon those targets*; units as indicated

	11/7/24	4Q24	1Q25	2Q25	3Q25
Breakevens (bp)					
5Y	242	240	235	225	220
10Y	236	235	230	225	220
30Y	233	230	230	225	220
Real yields (%)					
5Y	1.77	1.85	1.70	1.65	1.60
10Y	1.98	2.15	2.05	1.90	1.90
30Y	2.23	2.45	2.35	2.20	2.30

* Targets for real yields are based on our nominal yield forecasts and breakeven targets
Source: J.P. Morgan

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Trade recommendations

- **Maintain 5-year beta-weighted breakeven wideners paired with energy hedge**

- Stay long 100% risk, or $113mn notional of TII 2.125% Apr-29s
- Stay short 65% risk, or $77.9mn notional of T 4.625% Apr-29s
- Stay short 29 Brent futures (COF5)
(See *US Treasury Market Daily*, 10/17/24). P/L since inception: -4.5bp

Figure 14: Trade performance over the past 12 months

P/L reported in bp of yield unless otherwise indicated

TRADE	ENTRY	EXIT	P/L
2Yx3Y inflation swap longs	10/4/2024	10/9/2024	8.8
Hedged 5s/10s BE curve steepener	9/13/2024	10/4/2024	-3.3
5Yx5Y inflation swap longs	8/16/2024	8/28/2024	4.5
1Yx1Y inflation swap longs	6/14/2024	7/10/2024	17.5
Jul 24/Jul 25 BE wideners	5/10/2024	5/28/2024	11.7
10Yx20Y breakeven wideners	4/12/2024	4/26/2024	4.7
Long 5Y TIPS	3/20/2024	4/25/2024	-31.0
6mx1Y breakeven wideners	4/5/2024	4/19/2024	7.3
Old 10s/30s breakeven curve steepeners	2/23/2024	4/12/2024	-5.6
Long 1Y inflation swaps (hedged)	3/8/2024	4/5/2024	7.0
5-year TIPS longs	2/9/2024	3/7/2024	9.9
10-year energy-hedged BE narrowers	1/19/2024	1/30/2024	7.5
30-year breakeven narrowers	11/9/2023	12/7/2023	21.7
AGGREGATE:			
Number of trades	13		
Number of winners	10		
Hit ratio	77%		
Aggregate P/L (bp of yield)	60.7		

Source: J.P. Morgan

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Interest Rate Derivatives

Elephant spirits

- The election resulted in the Republican party winning the Presidency as well as the Senate, and likely the House. Given such a clear Red sweep, yields rose and risky assets outperformed reflecting some combination of animal spirits, lower future tax rates and anticipation of de-regulatory tailwinds
- The widening in swap spreads is not obviously consistent with the implications of a Red sweep (which is likely to bring larger deficits and upside risk to UST duration supply). It is likely a reflection of deregulatory optimism, particular with regards to SLR relief for US Treasuries. Technical adjustments to SLR are likely not at the top of the de-regulatory agenda, and is unlikely to materialize in the near term even if it were. Moreover, with leverage not binding now as it was in 2020, resulting impacts on swap spreads would likely be minor. Thus, this week's widening move seems both exaggerated and premature
- Additionally, this week's FOMC meeting brought forth no indication of a near-term halt to QT, and we now look for QT to continue for three more months till the end of 1Q25. On the margin, the resulting deferral of reinvestment demand and the continuing downside pressure on Reserves and RRP balances (which in turn will likely maintain upward pressure on financing rates) together support a narrowing bias on swap spreads. Given this, given exaggerated optimism with respect to SLR, and given that upside risks to deficits are not yet fully priced into spreads, we now recommend re-entering swap spread narrowers in longer maturities and spread curve flatteners
- With the passing of significant event risk, a decline in short expiry implied volatility is to be expected, but this week's decline was in excess of what we had expected. Options markets are now likely underpricing the ~4bp/day pickup in realized volatility that is typical in the weeks following an election. Additionally, next week's economic data could prove significant as well. Therefore, given cheaper implieds and the potential for delivered volatility to remain elevated, we remain tactically bullish on short-expiry volatility

Elephant spirits

The highlight of this past week was of course the election, which resulted in the Republican party winning the Presidency as well as the Senate. Control of the House remains as yet undecided but Republican control is seen as highly likely. Given such a clear Red sweep, markets responded by pushing yields higher and the curve steeper on Wednesday. Risky assets outperformed significantly across the board, reflecting some combination of animal spirits, lower future tax rates and the anticipation of de-regulatory tailwinds (**Figure 1**).

These market moves are generally consistent with consensus views regarding the implications of a Red sweep. But the move in swap spreads was arguably less so. A Red sweep would likely bring larger deficits and therefore upside risks to UST duration supply, perhaps even earlier than our current outlook for coupon auction sizes to increase beginning a year from now (see US Treasury Market Daily: Post-election post-mortem: Fade belly cheapening for soft long exposure, maintain beta-weighted 5y breakeven longs, J. Barry et al., 11/6/2024). This would imply upside pressure on term funding premium, and a resulting narrowing bias on swap spreads as well as a spread curve flattening bias. But instead, swap spreads have widened significantly after the election, in roughly parallel fashion, by 3-5bp (**Figure 2**) which is unusually large for a weekly move. It is also worth noting that this wid-

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ening in swap spreads comes despite the fact that the FOMC statement on Thursday brought no signs of a near term cessation of QT. In other words, the ongoing shrinkage of Reserves / RRP balances and the also-ongoing lack of reinvestment demand from the Fed will both remain sources of narrowing pressure on swap spreads.

Figure 1: Yields were higher after the election but reversed on Thursday, while risky assets outperformed across the board

Nov 1st, Nov 6th and Nov 7th levels for select SOFR swap yields (%), 2s10s UST curve (%), and equity indices (SPX Index and BKX* Index)

		1-Nov	6-Nov	7-Nov
SOFR Swap Yields (%)	2Y	3.96	4.06	4.01
	5Y	3.83	3.92	3.85
	10Y	3.84	3.92	3.85
	30Y	3.71	3.77	3.73
UST (bp)	2s10s	16	16	12
Equity	SPX Index	5729	5929	5973
	BKX Index	122	135	131

*BKX Index is the KBW Bank Index
Source: J.P. Morgan., Bloomberg Finance L.P.

Figure 2: Swap spreads have widened across the curve in roughly parallel fashion

Selected statistics for maturity matched SOFR swap spreads, 11/1- 11/7; bp

	start	chg	end	min	mean	median	max
2Y	-23.4	3.4	-20.0	-23.4	-21.7	-22.0	-20.0
3Y	-28.6	4.3	-24.3	-28.6	-26.4	-26.8	-24.3
5Y	-38.0	4.0	-34.0	-38.0	-36.3	-37.1	-34.0
7Y	-46.6	4.0	-42.6	-46.6	-45.0	-45.4	-42.6
10Y	-52.6	3.0	-49.6	-52.6	-51.3	-51.7	-49.6
20Y	-80.5	5.4	-75.1	-80.5	-77.7	-78.3	-75.1
30Y	-84.5	3.0	-81.6	-84.5	-83.2	-83.6	-81.6

Source: J.P. Morgan.

Seen in this light, **this week's widening move in swap spreads appears to reflect a measure of de-regulatory optimism, particularly with regards to SLR relief for US Treasuries**. Indeed, the potential for a UST-exclusion from bank leverage capital rules has been a topic of much speculation among market participants this week. Such speculation is hardly unfounded - indeed, it was granted on a temporary basis after the onset of the pandemic, and has recently been discussed at the TBAC (see US Treasury Market Daily: November refunding review, J. Barry et al., 10/30/24). As such, it is certainly a possibility. But to the extent that this week's spread widening is a reflection of such an expectation, we see this as exaggerated and unlikely to materialize on a reasonable timeframe, for several reasons. **First**, even if banking system regulatory reforms are plausible and deemed a priority, technical adjustments to SLR are unlikely to be at the top of the list, given larger impacts from a number of other elements of the Basel III "endgame" agenda. **Second**, the timeline is hardly imminent - with several months to go before the new administration takes effect, followed by additional time to appoint key personnel and then navigate the rulemaking process, the timelines to enacting SLR reform seem lengthy at best, and are unlikely to impact the financing of USTs in the short run. **Third**, and perhaps most important, the impact of a UST exclusion from leverage capital was very impactful in 2020 because the pandemic-era QE produced sudden and sharp increases in bank leverage, making SLR a significantly binding constraint for the banking system. With ~2.5 years of QT now behind us and the Fed's balance sheet ~$2Tn smaller than its peak, leverage is no longer as binding and any relief on this front is likely to be marginal in its impact in the near term. **Therefore, all in all, we see this week's move in swap spreads as both exaggerated and premature**.

Separately, this week's FOMC meeting delivered a 25bp rate cut as expected, but brought forth no indications of a halt to QT. We have held the view that although Reserves are at elevated levels, their empirical stickiness, and the now-similar stickiness of RRP balances together combine to create tighter funding conditions (see Déjà vu awaits in funding markets). As such, we had expected the Fed to announce an end to QT no later than this meeting. Given that such an announcement has not occurred, we now modify our Fed balance sheet forecast - **we now look for QT to continue for three more months, and come to a halt by the end of 1Q25** (**Figure 3**). On the margin, **this is also supportive of a narrow-**

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ing bias in swap spreads, since it implies continuing tail risk of a rise in repo rates, and also means that any reinvestment demand for USTs from the Fed will be slower to materialize. **Given this,given what we see as premature and exaggerated SLR optimism, and given the fact that deficit risks are consequently being underpriced into swap spreads, we recommend re-entering swap spread narrowers (especially in longer maturities) and spread curve flatteners going forward** (see Trade recommendations).

Figure 3: We now look for QT to continue for three more months, and come to a halt by the end of 1Q25

Current* and projected total Fed balance sheet assets, RRP, TGA, Reserves, and Commercial bank deposits** through 1Q 2025, $bn

End-of-the-month	Fed Assets	RRP			TGA	Reserves	Commercial Bank Deposits
		O/N RRP	Foreign RRP	Total RRP			
Current	7045	166	389	555	842	3274	17666
Nov-24	6981	188	389	577	775	3255	17701
Dec-24	6917	214	389	603	700	3240	17739
Jan-25	6859	161	389	550	750	3185	17745
Feb-25	6818	206	389	595	650	3199	17806
Mar-25	6775	249	389	638	550	3213	17867

* Current as of 11/7/2024 Fed H.4. release
** Deposits as of 11/1/2024 Fed H.8. release
Source: J.P. Morgan., FRED, Federal Reserve H.4.1, Federal Reserve H.8

Implied volatility declined significantly over the past week with the passing of the election and the FOMC meeting, with shorter expiry swaptions leading the way (**Figure 4**). With the passing of significant event risk, a decline in short expiry implieds is to be expected. In our last publication, we had discussed the event risk priced into implieds for this week, and we estimated that implied volatility would decline by about 0.3 to 0.7 bp/day across different expiries and tails by the end of this week (see Purple rain). As Figure 4 shows, the decline we got this week was much in excess of what we had expected.

Looking ahead, **we continue to maintain a tactically bullish stance on gamma**. **One**, we think this week's decline in implieds is overdone and the options markets are now likely underpricing the ~4 bp/day pickup in realized volatility that markets have typically experienced in the weeks after an election (**Figure 5**). This is likely because the weeks immediately following an election are often dense with new information - whether related to policy or key personnel who will drive the new administration's agenda. **Additionally**, next week's economic data has the potential to be impactful, as markets turn their focus to CPI and retail sales. Therefore, **given cheaper implied volatility levels and given the potential for delivered volatility to remain elevated for the next few weeks, we remain tactically bullish on short-expiry volatility**.

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Figure 4: Implieds declined in excess of what we expected with the passing of this week's event risk

Swaption implied volatility as of 10/31 and 11/7, change over the week, expected change* and excess change **; bp/day

	Implied levels		Actual	Expected	Excess
	31-Oct	7-Nov	Chg	Chg	Chg
1Mx5Y	8.96	7.18	-1.78	-0.35	-1.43
1Mx10Y	8.64	6.67	-1.97	-0.34	-1.63
1Mx30Y	8.02	6.24	-1.77	-0.75	-1.02
3Mx5Y	7.78	7.06	-0.72	-0.24	-0.48
3Mx10Y	7.35	6.59	-0.76	-0.25	-0.51
3Mx30Y	6.81	6.16	-0.65	-0.37	-0.28

*Expected change in implied volatility is calculated using the 1-day breakevens from the FOA (Forward Option Agreement) inter-dealer market which we used used to estimate volatility around the election week (see Purple rain for details on the daily implied volatility around election week and methodology)
**Excess change is calculated as the difference between actual change and excess change
Source: J.P. Morgan.

Figure 5: Realized volatility has tended to increase in the weeks following an election

Pickup in realized volatility around the 2016 and 2020 elections*

	2016	2020	Average
1Mx5Y	4.1	2.7	3.4
1Mx10Y	4.6	4.5	4.5
1Mx30Y	4.6	4.1	4.3
3Mx5Y	4.3	2.8	3.6
3Mx10Y	4.5	4.7	4.6
3Mx30Y	4.7	4.1	4.4

*Calculated as the difference in 2-week standard deviation of daily changes in the underlying yields pre and post election in 2016 and 2020
Source: J.P. Morgan.

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Trading Recommendations

- **Initiate 2s/30s maturity matched swap spread curve flatteners**
  A red sweep would likely bring larger deficits and upside risk to UST duration supply, causing upward pressure on term funding premium, which biases us towards narrower swap spreads and a flatter swap spread curve. Moreover, this weeks widening moves around deregulatory optimism seem to be overdone, and any SLR relief is unlikely to materialize in the near term. Lastly, the FOMC meeting has not indicated any halt to QT in the near term, causing a potential tail risk of a rise in repo rates.
  -Pay fixed in 4.125% Oct 31 2026 maturity matched SOFR swap spreads. Buy $100mn notional of the 4.125% Oct 31 2026 (yield: 4.218%, PVBP: $187.7/bp per mn notional), and pay fixed in $96.6mn notional of a maturity matched SOFR swap (coupon: 4.018%, PVBP: $194.3/bp per mn notional) at a swap spread of -20.0bp.
  -Receive fixed in 4.5% Nov 15 2054 maturity matched SOFR swap spreads. Sell $11.6mn notional of the 4.5% Nov 15 2054 (yield: 4.543%, PVBP: $1620.9/bp per mn notional), and receive fixed in $10.6mn notional of a maturity matched SOFR swap (coupon: 3.726%, PVBP: $1777.5/bp per mn notional) at a swap spread of -81.7bp.
- **Stay long in 3Mx10Y straddles on a delta-hedged basis**
  P/L on this trade is currently -11.5abp. For original trade write up, see Fixed Income Markets Weekly 2024-11-01.
- **Stay long 65% risk weighted 1Yx10Y swaption volatility versus selling 1Y forward 2Yx10Y swaption volatility, synthetically constructed via suitably weighted 1Yx10Y and 3Yx10Y swaptions**
  P/L on this trade is currently -1.7abp. For original trade write up, see Fixed Income Markets Weekly 2024-10-18.
- **Maintain conditional exposure to a steeper 2s/10s curve in a rally using 3M expiry receiver swaptions, financed by selling 24% risk-weighted receiver swaptions on 7-year tails**
  P/L on this trade is currently -1bp. For original trade write up, see Fixed Income Markets Weekly 2024-09-13.

Closed trades over the past 12 months

P/L reported in bp of yield for swap spread, yield curve and misc. trades, and in annualized bp of volatility for option trades, unless otherwise specified

Note: trades reflect Thursday COB levels, and unwinds reflect Friday COB levels

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Trade	Entry	Exit	P/L
Spreads and basis			
5s/10s swap spread curve flatteners, paired with a 10% risk-weighted 5s/10s Treasury curve flattener	10/13/2023	12/8/2023	1.2
FV/UXY invoice spread curve flatteners , paired with a 10% risk-weighted FV/UXY Treasury futures curve flattener	10/13/2023	12/8/2023	1.7
Initiate swap spread narrowers in the 2Y sector	11/3/2023	12/8/2023	3.9
Initiate swap spread wideners in the 5Y sector	11/3/2023	12/8/2023	(3.2)
Initiate 20s/30s swap spread curve flatteners hedged with a 35% risk-weighted 20s/30s Treasury curve flattener	9/29/2023	1/5/2024	0.2
Initiate 3s/5s swap spread curve flatteners	12/8/2023	1/5/2024	0.9
Initiate swap spread wideners in the 5Y sector	1/5/2024	1/19/2024	4.2
Pay in 1.375% Nov '31 maturity matched swap spreads paired with 5% risk in 5s/10s OTR Treasury curve steepeners	1/10/2024	1/26/2024	2.4
Initiate 5s/30s swap spread curve flatteners	12/15/2023	2/2/2024	3.8
Initiate swap spread narrowers in the 30Y sector	1/5/2024	2/2/2024	0.2
Maintain a widening bias on swap spreads in the belly but switch to the 2.625% Feb 2029 issue	1/19/2024	2/23/2024	2.4
Maintain a widening bias on swap spreads in the belly using the 2.625% Feb 2029 issue, but hedge the narrowing risk from higher implied volatility with a long in 2Yx2Y swaption straddles	1/19/2024	2/23/2024	2.7
Initiate 2s/5s (100:60 weighted) maturity matched swap spread curve steepeners	1/26/2024	2/23/2024	(3.3)
Pay-fixed in 2.125% May '26 maturity matched swap spreads	3/15/2024	3/22/2024	3.6
Pay-fixed in 1.875% Jul '26 maturity matched swap spreads	3/22/2024	4/5/2024	3.4
Initiate 20s/30s 1.33:1 wtd maturity matched spread curve steepeners hedged with a 30% risk weighted 20s/30s steepener, but use an equi-notional blend of the Nov 53s and Aug 53s to create a synthetic approximate par bond in the 30Y leg	2/23/2024	4/12/2024	(2.5)
Initiate 30Y swap spread wideners	3/15/2024	4/12/2024	(0.1)
Pay in 4% Jan '27 maturity matched swap spreads	4/5/2024	4/26/2024	2.2
Initiate 10Y swap spread wideners using the Nov '33 issue	3/8/2024	5/17/2024	0.9
Initiate exposure to a steeper 7s/10s 1:0.75 weighted swap spread curve, and we recommend implementing the 7Y narrower leg with TYM4 invoice spreads	5/10/2024	5/28/2024	0.3
Initiate 1:0.9 risk weighted 20s/30s maturity matched swap spread curve steepeners	5/31/2024	6/14/2024	3.9
Initiate 5s/10s off-the-run swap spread curve steepeners (100:60 weighted)	3/8/2024	7/12/2024	(4.7)
Initiate 7s/10s swap spread curve steepeners paired with 25% risk in a 7s/10s UST curve steepener	3/22/2024	7/12/2024	(0.2)
Pay in Feb 2037 maturity matched swap spreads versus receiving in USU4 invoice spreads	6/14/2024	7/12/2024	0.8
Buy Feb 37s versus selling USU4 Futures	6/14/2024	7/12/2024	2.7
Pay-fixed in 1.875 Feb 2027 maturity matched swap spreads	4/26/2024	7/26/2024	(5.9)
Initiate 5s/30s spread curve flatteners	5/3/2024	7/26/2024	5.1
Pay-fixed in 4% Feb 2034 maturity matched swap spreads	5/17/2024	7/26/2024	(6.7)
Initiate 10s/30s swap spread curve flatteners	7/26/2024	8/2/2024	(0.8)
Initiate TU/TY invoice spread curve flatteners (1:0.35 weighted)	6/7/2024	8/23/2024	(6.3)
Pay-fixed in 4.625% Feb '26 maturity matched swap spreads	5/31/2024	9/6/2024	0.3
Pay-fixed in 4.375% Aug '28 maturity matched swap spreads	5/31/2024	9/6/2024	(1.8)
Initiate 10Y swap spread narrowers	8/16/2024	9/6/2024	2.5
Initiate 3s/7s swap spread curve flatteners	8/16/2024	9/6/2024	1.4
Initiate 0.875% June 2026 / 0.875% September 2026 swap spread curve flatteners	8/16/2024	9/6/2024	1.3
Initiate 5s/30s swap spread curve flatteners	8/23/2024	9/6/2024	(0.3)
Initiate 7s/20s weighted swap spread curve steepeners	8/23/2024	9/20/2024	3.8
Initiate 100:80 weighted 20s/30s maturity matched swap spread curve flatteners	9/6/2024	9/20/2024	2.3
Initiate 7s/10s maturity matched swap spread curve steepeners	9/27/2024	10/4/2024	0.0
Initiate 1:0.75 risk weighted 7s/10s maturity matched swap spread curve steepeners	5/31/2024	10/18/2024	0.8
Initiate 2s/3s maturity matched swap spread curve flatteners	9/20/2024	11/1/2024	0.0
Initiate 3s/30s maturity matched swap spread curve flatteners	10/4/2024	11/1/2024	(2.1)

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Duration and curve	Entry	Exit	P/L
Initiate 2Y fwd 2s/5s curve flatteners paired with 25% risk in a 1st/5th SOFR futures curve flattener	11/03/23	11/22/23	5.8
Initiate 6M fwd 5s/15s curve flatteners paired with equal risk in 3Y fwd 2s/15s steepeners	11/03/23	11/22/23	4.6
Buy the belly of a 40:65 weighted Z4/Z5/Z6 3M SOFR futures butterfly	11/03/23	11/22/23	5.6
Initiate 9M fwd 1s/10s flatteners paired with a 50% risk weighted long in March 2025 3M SOFR futures	11/09/23	11/22/23	15.8
Initiate 3Mx1Y / Greens weighted flattener (1:0.8 weighted) paired with 80% risk in a 3M forward 2s/10s swap curve steepener	01/05/24	01/26/24	2.9
Initiate U5/M6 SOFR futures curve flatteners paired with 110% of the risk in Z5/U6 3M SOFR futures curve steepeners	12/15/23	02/02/24	1.6
Buy the belly of a 35:65 weighted H5/H6/Z6 3M SOFR futures butterfly	12/15/23	02/02/24	1.9
Initiate 1Yx2Y / 3Mx30Y swap yield curve steepeners paired with 65% risk in a Reds / 10Yx5Y swap yield curve flattener	01/19/24	02/02/24	1.1
Receive fixed in the belly of a 6M forward 2s/7s/30s swap butterfly (40:69 weighted)	01/19/24	02/02/24	0.1
Initiate conditional exposure to a composite flattener in a selloff by buying 3Mx2Y payer swaptions (100% risk) versus selling 3Mx5Y and 3Mx30Y payer swaptions (24% and 100% risk respectively)	02/02/24	02/23/24	14.3
Buy H5 and Z5 3M SOFR futures contracts (30:100 weighted) versus selling U4 3M SOFR futures contracts (100% risk weight) and pay-fixed in 6M forward 10Y swaps (40% risk weight)	02/09/24	02/23/24	5.8
Initiate exposure to rising term premium by selling the belly of a 35/65 weighted 3M forward 5s/10s/15s butterfly	12/08/23	03/08/24	(1.5)
Initiate SFRM5 / Blues flatteners paired with a 110% risk weighted 3M forward 2s/10s steepener	03/01/24	03/22/24	3.3
Initiate 3M forward 3s/20s swap curve steepeners, paired with 85% of the risk in a SFRM5 / 3Mx10Y curve flattener	03/08/24	04/05/24	3.2
Initiate 2Y forward 2s/5s swap curve steepeners paired with 40% risk in 3M forward 2s/5s flatteners	01/26/24	04/12/24	(11.4)
Initiate conditional exposure to a flatter 2s/5s swap yield curve in a selloff using 3M expiry payer swaptions	03/22/24	04/12/24	5.2
Initiate conditional exposure to a flatter 18M/5Y swap yield curve in a selloff using 6M expiry payer swaptions	04/05/24	04/12/24	3.1
Initiate conditional exposure to a flatter 1s/5s swap yield curve in a selloff using 3M expiry payer swaptions	02/23/24	04/26/24	(9.4)
Initiate 1Y forward 2s/5s swap curve flatteners, paired with weighted longs in H5 and H6 3M SOFR futures (20% and 10% respectively)	03/22/24	04/26/24	(9.5)
Initiate SFRM5 / 3Mx5Y flattener, hedged with a 20% risk weighted long in Reds	04/05/24	04/26/24	(5.0)
Initiate 5th/9th SOFR futures curve flatteners hedged with a risk weighted amount 2Y forward 2s/5s swap curve steepeners	04/12/24	05/03/24	3.0
Receive in the belly of a 0.625/1.0/0.375 weighted 3M forward 2s/7s/20s swap butterfly, with an additional 15% risk weighted long in June 2024 3M SOFR futures	02/23/24	05/17/24	2.7
Initiate 3M forward 2s/3s swap curve flatteners hedged with a 14% risk weighted long in the M4 3M SOFR futures	02/23/24	05/17/24	0.4
Initiate 3M forward 5s/15s swap curve flatteners paired with 70% risk in a 2Y forward 2s/20s swap curve steepener	03/22/24	05/17/24	2.8
Buy the belly of a 2s/5s/15s weighted swap butterfly (50:50 weighted)	04/12/24	05/17/24	2.4
Initiate 3M forward 1s/3s swap curve flatteners, hedged with a 65% risk weighted long in the 3Mx3M sector and a 25% risk weighted short in the 15Mx3M sector	05/03/24	05/17/24	2.1
Buy the belly of a U5/M6/H7 SOFR Futures butterfly (-0.37:1:-0.63 risk weighted)	03/01/24	05/31/24	(0.7)
Initiate a Greens/Blues steepener paired with 55% of the risk in a SFRM5 / 3Mx5Y swap curve flattener	03/15/24	05/31/24	2.2
Buy the belly of a Z5/U6/H7 3M SOFR futures butterfly (-0.33:1.0:-0.67 risk weighted)	04/19/24	05/31/24	1.8
Initiate 12Mx3M / 3Mx10Y flatteners, paired with 33% risk in a 3Mx2Y receive fixed swap	05/17/24	06/06/24	5.7
Initiate 3M fwd 3s/15s flatteners paired with 85% risk in 2Y fwd 3s/30s steepeners	05/17/24	06/06/24	4.5
Initiate 3Mx1Y / 2Yx1Y forward swap curve flatteners as a bullish proxy	05/31/24	06/06/24	11.5
Initiate 3Mx1Y / 2Yx1Y swap curve flatteners paired with 45% risk-weighted pay-fixed positions in 3Mx5Y swaps	05/31/24	06/06/24	0.0
Initiate conditional exposure to a flatter 1s/2s swap yield curve in a rally using 1Y expiry receiver swaptions	04/05/24	06/14/24	4.0
Initiate Z5/U6 SOFR futures flatteners paired with H6/Z6 SOFR futures steepeners (0.85:1 risk weighted)	03/01/24	07/12/24	1.8
Initiate conditional exposure to a steeper 10s/20s swap yield curve in a selloff using 9M expiry payer swaptions	03/15/24	07/12/24	4.0
Initiate 3M forward 10s/15s swap curve steepeners paired with 25% risk in 3M forward 3s/7s flatteners	04/26/24	07/12/24	3.5
Initiate 3M forward 10s/30s steepeners (1:1.5 risk weighted) paired with M5/Z5 3M SOFR futures flatteners	06/07/24	07/12/24	2.9
Initiate 15Mx3M / 1YX1Y forward swap curve flatteners, paired with 20% of the risk in a long in 18Mx3M and a 24% risk weighted short in 3Mx5Y forward swaps	05/03/24	08/02/24	(1.3)
Receive in 3Mx3Y and 3Mx5Y swaps versus paying in 3Yx1Y and 12Mx3M swaps	06/14/24	08/02/24	(8.8)
Initiate a synthetic 6M forward 2s/10s swap curve steepener, constructed by replacing the 2Y leg with a 6Mx3M / 18Mx3M flattener	07/12/24	08/02/24	(28.9)
Initiate a synthetic 3M forward 5s/30s swap curve steepener, constructed by replacing the 5Y leg with a 3Mx3M / 3Mx2Y flattener	07/26/24	08/02/24	(18.1)
Initiate conditional exposure to a flatter 1s/2s swap yield curve in a rally using 6M expiry receiver swaptions	07/26/24	08/02/24	(8.8)
Initiate conditional exposure to a flatter 1s/7s swap yield curve in a selloff using 6M expiry payer swaptions	07/12/24	10/04/24	(6.6)
Initiate conditional exposure to a flatter 1s/3s swap yield curve in a selloff using 3M expiry payer swaptions	09/13/24	10/04/24	0.4
Initiate Greens / 3Mx15Y flatteners (0.9:1.0 weighted)	09/20/24	10/04/24	6.1
Initiate conditional exposure to a flatter 1s/5s swap yield curve (100:102 weighted) in a selloff using 3M expiry payer swaptions	09/20/24	10/04/24	11.0

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Options	Entry	Exit	P/L
Initiate short gamma exposure in the 6Mx30Y sector	11/03/23	12/08/23	7.9
Sell 6Mx30Y swaption straddles versus buying a vega-neutral amount of 1Yx30Y swaption straddles	11/03/23	12/08/23	0.4
Initiate long gamma exposure in the 1Yx10Y sector	12/08/23	02/23/24	(2.1)
Initiate long exposure to 2Yx2Y volatility with a suitably weighted short in July Fed funds futures to hedge the downside risk from a fall in Fed-easing expectations	01/05/24	02/23/24	2.6
Overweight 2Yx2Y swaption straddles versus a vega-neutral amount of 5Yx5Y swaption straddles	01/19/24	02/23/24	3.2
Overweight 6Mx10Y swaption straddles versus selling 110% of the vega risk in 1Yx10Y swaption straddles	01/26/24	02/23/24	1.3
Buy 6Mx10Y straddles	03/01/24	03/08/24	(6.6)
Initiate longs in 6Mx10Y swaption implied volatility, delta hedged daily	03/15/24	03/22/24	(5.1)
Overweight 6Mx2Y swaption straddles versus a theta-neutral amount of 6Mx5Y swaption straddles	01/19/24	04/12/24	(8.8)
Sell 2Yx30Y swaption volatility versus buying 50% of the vega risk in 2Yx2Y swaption volatility , and pay fixed in 2Yx 10Y swaps to neutralize the bullish bias in this trade	02/23/24	04/12/24	1.5
Buy 6Mx10Y volatility versus 6M forward 6Mx10Y volatility, synthetically constructed via suitably weighted 1Yx10Y and 6Mx10Y swaptions	04/05/24	04/12/24	3.2
Buy 2Yx5Y swaption straddles on a delta hedged basis	04/12/24	04/19/24	1.0
Sell 6Mx10Y straddles on a delta hedged basis	04/26/24	05/03/24	3.1
Sell 6Mx15Y straddles on a delta hedged basis	05/03/24	05/10/24	(1.6)
Sell 1Yx2Y volatility versus buying a theta neutral amount of 1Yx5Y volatility	05/17/24	06/06/24	0.6
Initiate Fronts/Green curve flatteners, paired with delta hedged long volatility positions in the 1Yx10Y swaption sector	05/31/24	06/06/24	5.6
Initiate exposure to long curve volatility by buying 6Mx2Y and 6Mx10Y straddles (41:60 vega weighted) versus selling 6Mx5Y straddles	12/08/23	06/07/24	1.1
Buy 2Yx5Y swaption straddles on a delta hedged basis, versus 6Mx1Y / 18Mx1Y flatteners	06/07/24	06/14/24	3.6
Initiate outright shorts in 3Yx30Y swaption implied volatility, but delta hedge monthly or if rates move by over 25bp in either direction since the last delta hedge	03/08/24	07/12/24	(5.0)
Buy 1Yx30Y volatility versus 1Y forward 1Yx30Y volatility, synthetically constructed via suitably weighted 2Yx30Y and 1Yx30Y swaptions	03/15/24	07/12/24	(2.5)
Buy 65% risk weighted 1Yx10Y swaption volatility versus selling 1Y forward 2Yx10Y swaption volatility, synthetically constructed via suitably weighted 1Yx10Y and 3Yx10Y swaptions	04/12/24	07/12/24	(4.4)
Sell 6Mx10Y swaption straddles on a delta hedged basis, paired with a short position in Greens	06/14/24	07/12/24	2.2
Buy 1Yx5Y straddles versus selling vega-neutral amount of 5Yx5Y straddles	07/12/24	08/02/24	4.7
Buy A+100 1Yx5Y payer swaptions and sell A-100 1Yx5Y receiver swaptions, delta-hedged daily, to position for a correction in skew	04/19/24	08/23/24	(8.5)
Buy 6Mx5Y swaption straddles versus selling 150% of the vega risk in 6Mx30Y straddles	07/12/24	09/13/24	2.2
Initiate longs in 6Mx5Y swaption implied volatility on an outright basis, delta hedged daily	08/02/24	09/13/24	(8.5)
Overweight 6Mx5Y and 6Mx30Y swaption volatility (vega weights of 0.32 and 0.76, respectively) versus selling 6Mx10Y swaption volatility	04/05/24	10/04/24	(1.2)
Buy 3Yx3Y versus selling 10Yx10Y swaption straddles	09/06/24	10/04/24	(5.6)
Buy 1Yx10Y swaption straddles on a delta hedged basis coupled with a weighted long in S&P 500 futures	09/13/24	10/04/24	1.2
Overweight 1Yx10Y straddles versus a gamma-neutral amount of 1Yx15Y straddles	05/03/24	10/18/24	(2.1)
Buy 1Yx3Y versus selling 105% of the vega risk in 1Yx10Y swaption straddles	09/20/24	10/18/24	(0.2)
Sell 6Mx10Y straddles versus buying 130% of the vega weight in 6Mx30Y straddles	09/27/24	10/18/24	(0.3)
Buy 6Mx2Y swaption volatility versus selling a carry-neutral amount of 6Mx5Y swaption volatility	09/27/24	10/18/24	0.7
Sell 6Mx10Y straddles on a delta-hedged basis	10/04/24	10/18/24	(1.5)
Buy 6Mx2Y straddles on a delta-hedged basis	10/04/24	11/01/24	2.5
Others	**Entry**	**Exit**	**P/L**
Position for a widening in WN calendar spreads	11/9/2023	11/22/2023	1.8
Buy the USZ3/USH4 weighted calendar spread hedged with USZ3/WNZ3 Treasury futures curve flatteners	11/9/2023	11/22/2023	0.2
Position for a narrowing in FV calendar spreads	11/9/2023	11/22/2023	0.3
WN calendar spreads narrowers	2/13/2024	2/23/2024	(0.7)
UXY calendar spreads narrowers	2/13/2024	2/23/2024	(0.8)
TU calendar spreads narrowers	2/13/2024	2/23/2024	(0.3)
Sell the 4.75% Nov 2053 WNM4 basis, versus buying payer swaptions	3/8/2024	4/12/2024	1.0
Initiate calendar spread wideners in US Futures	5/17/2024	5/28/2024	(3.0)
Initiate calendar spread narrowers in UXY Futures	5/17/2024	5/28/2024	0.4
Initiate calendar spread narrowers in FV futures	5/17/2024	5/28/2024	1.0
Initiate calendar spread wideners in US Futures	8/16/2024	8/23/2024	(0.8)
Initiate calendar spread narrowers in FV Futures	8/16/2024	8/23/2024	(0.1)
Buy the USZ4 factor-weighted CTD basis	9/13/2024	9/20/2024	2.4
Buy the WNZ4 factor-weighted CTD basis	9/13/2024	9/20/2024	1.0
Total number of trades			**138**
Number of winners			**91**
Hit rate			**66%**

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Recent Weeklies	
01-Nov-24	Purple rain
25-Oct-24	Déjà vu awaits in funding markets
18-Oct-24	Counting down to November
04-Oct-24	Strong data, tighter liquidity conditions and rising geopolitical risk
27-Sep-24	Waiting Game
20-Sep-24	From Dovish Pause to Hawkish Easing
13-Sep-24	Schrodinger's Cut
06-Sep-24	Rates, unlike the economy, are not yet in "equipoise"
23-Aug-24	False Fall
16-Aug-24	Hopscotch
2-Aug-24	Powell sees the data, markets see one data point
26-Jul-24	Joie de Louvre
12-Jul-24	The Evitable Conflict
14-Jun-24	Pardon my French
07-Jun-24	The BOC and ECB begin a game of BOCCE-Ball, likely without the Fed for now
31-May-24	The planets, if not the stars, are aligning
17-May-24	Another brick in the vol
10-May-24	The election enters the hearts and minds of options traders
3-May-24	R2-P2
26-Apr-24	Perfectly priced to patience
19-Apr-24	Should I stay or should I go?
12-Apr-24	A hairpin bend on the road to easing
5-Apr-24	Shaken, not stirred
22-Mar-24	The Fed, walking a tightrope, finds better balance
15-Mar-24	(P)PI day
08-Mar-24	The sun is the same, in a relative way, but vol is lower
01-Mar-24	Governor Vol-ler moves the market
23-Fed-24	What's the rush?
09-Feb-24	Soft landings, TouchdoWNs, and Safety in the End Zone
02-Feb-24	When it rains, it pours
26-Jan-24	All eyes on Washington
19-Jan-24	Polar vortex duration extension
05-Jan-24	Happy new taper
15-Dec-23	On the second day of FOMC, my true dove spoke to me
8-Dec-23	What I tell you three times is true
9-Nov-23	The tail that wagged the market

Outlooks	
28-Jun-24	Interest Rate Derivatives 2024 Mid-Year Outlook: Waiting for someone or something to show you the way
21-Nov-23	Interest Rate Derivatives 2024 Outlook: Goodbye Hard Times, Hello Great Expectations?
Recent Special Topic Pieces	
13-Aug-24	US bond futures rollover outlook: September 2024 / December 2024
10-Jul-24	Trading Principal Factor Volatility
15-May-24	US bond futures rollover outlook: June 2024 / September 2024
29-Apr-24	Term Funding Premium and the Term Structure of SOFR Swap Spreads
13-Feb-24	US bond futures rollover outlook: March 2024 / June 2024
9-Nov-23	Death cab for QT
8-Nov-23	US bond futures rollover outlook: December 2023 / March 2024

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Short-Term Fixed Income

- Price action in the markets following this week's elections suggest stronger growth, higher inflation, looser fiscal policy, less stringent regulatory policy, and a higher landing place for the Federal Reserve
- While our US economists continue to expect a 25bp cut in December, they now anticipate quarterly 25bp rate cuts in 2025, as opposed to every meeting, until the fed funds rate reaches 3.5%
- A higher terminal rate should continue to position MMFs as an attractive liquidity investment vehicle relative to other cash alternatives, thereby keeping AUMs elevated
- Odds of a red sweep have increased, which should provide for a less contentious debt ceiling debate and a less protracted TGA drawdown. However, there is risk that the budget deficit could widen more relative to baseline expectations, and Treasury coupon sizes could increase larger and earlier than previously expected
- Considering the above, and the lack of any mention of any end to QT at the November FOMC meeting as well as declining ON RRP balances, we have pushed our QT end call to 1Q25
- We believe the decline on ON RRP balances QTD has been driven by increases in liquidity supply (e.g., T-bills and repo) alongside MMFs' desire to extend as a shallower easing cycle has been priced in
- Indeed, prime MMF WAMs and government MMF WAMs are now at 27 days and 35 days, compared to 23 days and 29 days respectively at September-end
- **Near-term catalysts**: CPI (11/13), PPI (11/14), Retail Sales (11/15)

Market commentary

As of the time of writing, the outcome of the House elections remains undecided, but Trump's decisive victory (both in terms of the electoral vote and the popular vote) and a Republican-controlled Senate suggest the odds of a red sweep are high. Equities rallied, the Treasury curve moved steeper before retracing later in the week, and the dollar was stronger. Price action in the markets following the elections suggest stronger growth, higher inflation, looser fiscal policy, less stringent regulatory policy, and a higher landing place for the Federal Reserve.

If a red sweep is realized, this could trigger major policy changes. From a legislative standpoint, our US economists note the two most immediate issues now is how assertively Trump pushes forward with his campaign pledges on immigration and trade. While there are minimal inflationary implications on the former, the same could not be said about the latter. The lesson from the first Trump presidency for the US on tariffs was higher import prices, a smaller increase in consumer prices, somewhat lower economic activity, and negative business sentiment offset by a less stringent regulatory backdrop. It's possible that all of the expiring provisions of the TCJA at the end of 2025 also get extended (See *Economic implications of the elections*, M. Feroli, 11/6/24).

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Against this backdrop, there are a number of implications for the short-term fixed income markets:

1. **Less aggressive Fed easing**: While we know some of the policies that Trump is focused on, the devil is in the details in terms of how they will unfold and what their impact would be on the economy. In a period of uncertainty, the Fed might move more slowly than it otherwise would. To that end, while our economists are still forecasting a 25bp cut at the December meeting (contingent on two CPI reports and the single jobs report released between now and then), we now see the Fed easing at a quarterly pace, with the next ease in March and continuing until the funds rate reaches 3.5%. Notably, at yesterday's FOMC meeting, despite providing no surprises in terms of lowering the fed funds target range to 4.50-4.75% and in the post-meeting statement, Chair Powell was questioned during the press conference if he would resign if asked by Trump, he said "No." When asked if he'd be legally required to leave, he had another simple one-word answer "No" (see *He's not leaving*, M. Feroli, 11/7/24).
2. **Less contentious debt ceiling debate**: Historically, the most contested debt ceiling debate has taken place under a Democratic President and a Republican-controlled House, like in 2011, 2013, 2015, and 2023. Given the outcome of the elections so far, any passage of a debt ceiling legislation should be well in advance of the "x-date". That said, our Treasury strategists believe that trade and immigration policy will likely take a greater priority before the debt ceiling is debated and that a debt ceiling resolution will come about by early 2Q25 (see *US Treasury Market Daily*, 10/28/24). Taken together, this gives way to a….
3. **Less protracted drawdown of the TGA**: The debt limit suspension is scheduled to expire on January 1, 2025. In prior episodes, Treasury would begin using extraordinary measures and drawing down funds in its TGA to meet financial obligations until the debt ceiling is raised or suspended again. Current figures suggest these measures/funds would be exhausted by July 2025 and Treasury would risk a technical default. However, given a more "unified" government and the likelihood that the debt ceiling debate is resolved earlier rather than later, our Treasury strategists believe this will bias TGA balances lower to $550bn in 1Q25 (assuming Treasury's $700bn TGA forecast for 4Q24) before Treasury brings TGA back up to more normal levels by the middle of next year (see *Post election post-mortem*, J. Barry, 11/6/24).
4. **More deregulation**: Given the precedent set forth by Governor Tarullo and Governor Quarles where both resigned as Vice Chair of Supervision following the handoff from the Obama to Trump and Trump to Biden administrations respectively, we believe it's possible that current Vice Chair of Supervision Michael Barr might do the same. It's unclear who would be the replacement, but Governor Bowman, a Republican nominated by Trump, is a potential contender. Notably, she has recently highlighted some issues with eSLR, namely how Treasury market intermediation can be disrupted by this known leverage rule. Importantly, this comes at a time when both policy makers and market participants are exploring ways to improve Treasury market functioning. In fact, at the November refunding, they discussed potentially exempting reserves and Treasuries from SLR, among other things. That being said, any rulemaking will need to be made in cooperation with the FDIC and the OCC, which could delay any meaningful changes (see *Post election post-mortem*, J. Barry, 11/6/24). The composition of other banking regulations (e.g., Basel III endgame, GSIB surcharge, enhanced liquidity regulations) and when they would be proposed or re-proposed is also somewhat unclear. But to the extent they are watered down, it could benefit banks (see *JPM Banks - Large Cap | Election 2024: Near-Term Optimistic Regulatory Expectations Key Driver; Medium-*

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Term Uncertainty from Macro Factors, V. Juneja, 11/7/24).

5. **Larger budget deficits and more Treasury supply**: Bipartisan research has noted that Trump's policy plans would increase the federal debt by $7.5tn during the 2026-2035 period. This should further widen Treasury's financing gap and prompt a need to once again increase Treasury coupon auction size to meet their funding needs. Moreover, a Republican sweep means the increase in coupon auction sizes could be larger than previously expected and also take place earlier than expected, potentially in August or even May of next year (see *Post election post-mortem*, J. Barry, 11/6/24).

What does this all mean? The combination of a higher terminal rate and what is likely going to be a higher term premium for Treasuries longer out the curve has prompted our Treasury strategists to revise their rate forecasts higher: they now expect 2y and 10y Treasuries to be at 4.25% and 4.50% respectively by YE24. We have also adjusted our EFFR and SOFR targets to reflect our new policy expectations for the coming year (Figure 15).

Figure 15: Our Treasury strategists have revised their rate forecasts higher, and we have also adjusted our EFFR and SOFR targets

J.P. Morgan interest rate forecast (%)

	4Q24 31 Dec	1Q25 31 Mar	2Q25 30 Jun	3Q25 30 Sep
Rates (%)				
EFFR	4.35	4.10	3.85	3.60
SOFR*	4.40	4.15	3.90	3.65
UST 2y	4.25	4.00	3.80	3.65
UST 3y	4.20	4.00	3.80	3.65
UST 5y	4.25	4.05	3.90	3.80
UST 7y	4.35	4.15	4.00	3.90
UST 10y	4.50	4.35	4.15	4.10
UST 20y	4.80	4.65	4.45	4.40
UST 30y	4.75	4.65	4.45	4.50

Source: J.P. Morgan

For the short-term markets, this repricing to a "higher-for-longer" scenario places MMFs and other liquidity investment vehicles in a better position than previously expected as rates should remain relatively high, particularly against bank deposits, which should leave the >$6tn of AUMs largely in place (Figure 16). In other words, MMFs should remain an attractive liquidity product relative to cash alternatives. It's possible that some money shifts out to the longer end of the curve, but we think that cash movement is limited relative to the overall size of the MMF complex.

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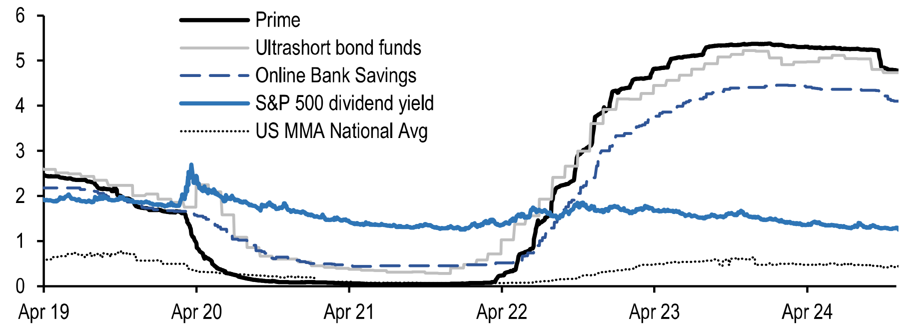
Figure 16: Prime MMFs still remain the most attractive liquidity product relative to cash alternatives, yielding at 4.78%

Selected yields (%)

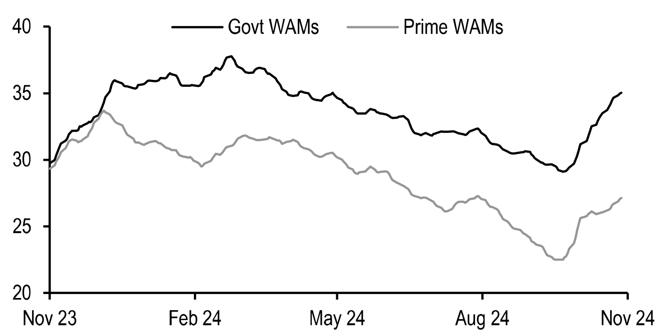


Source: Morningstar, Crane Data, Bloomberg, J.P. Morgan

Meanwhile, expectations of a higher terminal rate and a shallower easing cycle have resulted in a steepening of the very front-end of the Treasury yield curve (e.g., 1m1y and 3m2y are each at -21bp versus a local low of -100bp and -132bp in early September respectively). This should prompt liquidity investors to extend and add duration along the money markets curve. To be sure, this is a dynamic that was already in play even prior to the elections. Indeed, since the end of September, there has been a distinct upward trend in MMFs extending their maturities. Specifically, prime fund WAMs have increased by 5 days to reach 27 days, while government fund WAMs have risen by 6 days to 35 days (Figure 17). MMF WALs have also seen a significant rise (Figure 18). Volumes in 1-year fixed-rate bank CP/CD maturities have also increased (Figure 19).

Figure 17: Prime fund WAMs have increased by 5 days to reach 27 days, while government fund WAMs have risen by 6 days to 35 days

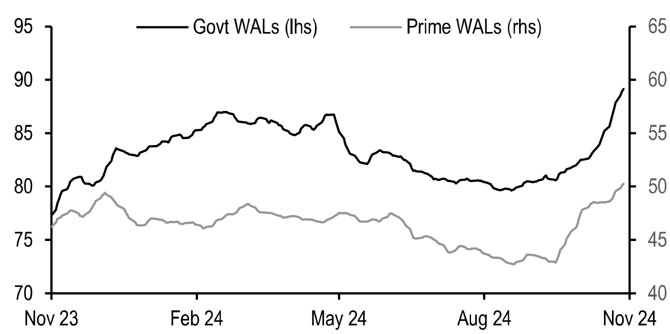
5-day average of prime and government fund WAMs (days)



Source: Crane Data, J.P. Morgan

Figure 18: MMF WALs have also seen a significant rise lately

5-day average of prime and government fund WALs (days)



Source: Crane Data, J.P. Morgan

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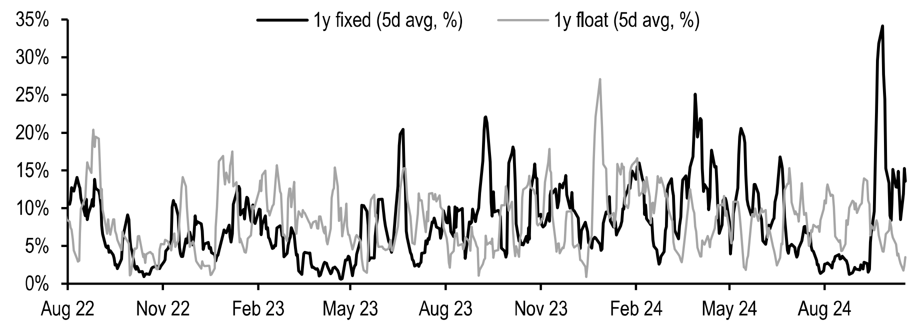
Figure 19: Short-term credit investors have extended further along the money market curve, particularly in 1-year fixed-rate bank CP/CD maturities

5-day average of bank CP/CD 1y fixed vs. FRN volumes as a percentage of total daily volumes (%)



Source: DTCC, J.P. Morgan

That said, despite the steepening, the curve still remains negatively sloping at this point. Given expectations of not only a shallower easing cycle but also a slower pace of easing, it's unclear when the curve will become positively sloping. It might take until 2H before that is realized, which at that point would provide a more meaningful support for cash to move out into the ultrashort/short-term fund space.

With respect to QT, liquidity conditions have normalized post October month-end (SOFR at 4.81%, TGCR at 4.81%, EFFR at 4.83%) as increases in both T-bill and repo supply (since 3Q: +$200bn for T-bills and +$32bn for TGCR volumes) alongside MMFs' desire to extend given shallower easing expectations have drawn cash out of the ON RRP facility (Figure 20). Current rates are well below IORB as opposed to at or above IORB, something Dallas Fed President Lorie Logan says she expects to see when liquidity is no longer abundant. But even if QT continues past year-end, we think it's unlikely to continue much further into 2025: reserves have been sticky at $3.2tn, there is only so much more room to run on ON RRP balances, and given what we expect to be a less contentious and protracted debt ceiling debate and TGA drawdown respectively, the Fed cannot rely on the debt ceiling to provide a temporary boost in reserves to extend the QT runway. We now think QT will end in 1Q25.

Furthermore, expected increases in coupon auction sizes to fund Treasury's growing financing needs, now at risk of larger and earlier increases given the red sweep, should continue to push SOFR towards the upper end of the fed funds corridor. Meanwhile, any form of deregulation is likely going to take time to unfold (given personnel changes and the rulemaking process) which means Treasury market intermediation will only become more challenging and continue to push dealers towards more balance sheet friendly structures (e.g., sponsored repo). Indeed, FICC repo volumes have grown substantially this year and will continue to grow, if not to comply with the Treasury clearing repo mandate by June 2026 (Figure 21).

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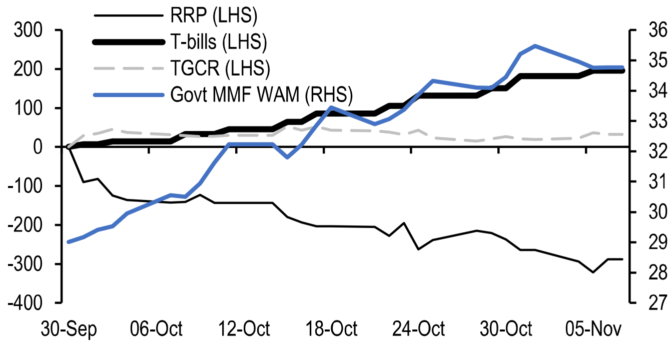
Figure 20: Repo and T-bill supply increase, more cash drawn out of ON RRP facility since the start of Q4

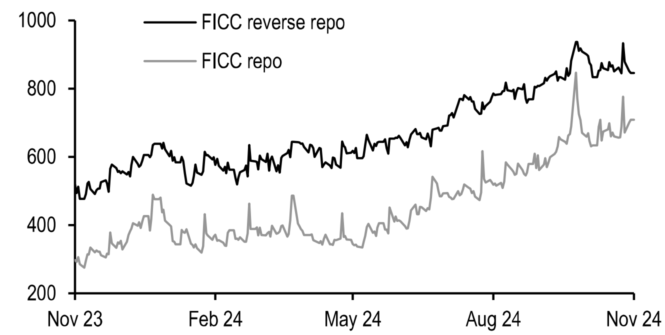
RRP, T-bill, and TGCR supply (LHS, $bn) and govt MMF WAMs (RHS, days)



Source: Crane Data, US Treasury, Federal Reserve, J. P. Morgan

Figure 21: FICC repo volumes surged this year, hitting a peak of over 840bn at September-end

FICC RRP and repo volumes ($bn)



Source: Federal Reserve

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Forecast & Analytics

Interest rate forecast

	Actual 7-Nov	1m ahead 7-Dec	4Q24 31-Dec	1Q25 31-Mar	2Q25 30-Jun	3Q25 30-Sep
Rates (%)						
Effective funds rate	4.83	4.58	4.35	4.10	3.85	3.60
SOFR	4.81	4.56	4.40	4.15	3.90	3.65
2-yr Treasury	4.22	4.20	4.25	4.00	3.80	3.65
3-yr Treasury	4.18	4.15	4.20	4.00	3.80	3.65
5-yr Treasury	4.19	4.20	4.25	4.05	3.90	3.80
7-yr Treasury	4.26	4.25	4.35	4.15	4.00	3.90
10-yr Treasury	4.34	4.35	4.50	4.35	4.15	4.10
20-yr Treasury	4.64	4.65	4.80	4.65	4.45	4.40
30-yr Treasury	4.54	4.55	4.75	4.65	4.45	4.50
Spreads (bp)						
Fed funds/2yr	-61	-38	-10	-10	-5	5
2s/10s	12	15	25	35	35	45
2s/5s	-3	0	0	5	10	15
5s/10s	15	15	25	30	25	30
5s/30s	35	35	50	60	55	70
10s/30s	20	20	25	30	30	40

Source: J.P. Morgan

Swap spread forecast*

SOFR Swap Spread (bp)	Actual 7-Nov-24	YE24 31-Dec-24
2-year SOFR swap spread (bp)	-20	-6
5-year SOFR swap spread (bp)	-34	-22
10-year SOFR swap spread (bp)	-49	-37
30-year SOFR swap spread (bp)	-81	-79

* Forecast uses matched-maturity spreads
Source: J.P. Morgan

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TIPS real yield & breakeven forecast

	Actual 7-Nov-24	4Q24 31-Dec-24	1Q25 31-Mar-25	2Q25 30-Jun-25	3Q25 30-Sep-25
Breakevens (bp)					
5Y	242	240	235	225	220
10Y	236	235	230	225	220
30Y	233	230	230	225	220
Real yields (%)					
5Y	1.77	1.85	1.70	1.65	1.60
10Y	1.98	2.15	2.05	1.90	1.90
30Y	2.23	2.45	2.35	2.20	2.30
Curves (bp)					
5s/10s BE	-6	-5	-5	0	0
10s/30s BE	-3	-5	0	0	0
5s/10s yld	22	30	35	25	30
10s/30s yld	25	30	30	30	40

Source: J.P. Morgan

Economic forecast

%ch q/q, saar, unless otherwise noted

	24Q1	24Q2	24Q3	24Q4	25Q1	25Q2	25Q3	2023*	2024*	2025*
Gross Domestic Product										
Real GDP	1.6	3.0	2.8	1.8	1.8	1.8	2.0	3.2	2.3	1.9
Final Sales	2.1	1.9	3.0	2.0	1.4	1.6	2.0	3.6	2.3	1.8
Domestic Final Sales	2.7	2.8	3.5	2.5	1.6	1.6	2.1	3.5	2.8	1.9
Business Investment	4.5	3.9	3.3	3.3	4.0	3.4	5.3	5.0	3.7	4.6
Net Trade (% contribution to GDP)	-0.6	-0.9	-0.6	-0.6	-0.3	-0.1	-0.1	0.1	-0.6	-0.1
Inventories (% contribution to GDP)	-0.5	1.1	-0.2	-0.2	0.4	0.2	0.0	-0.4	0.0	0.1
Prices and Labor Cost										
Consumer Price Index	3.8	2.8	1.2	3.2	2.4	1.7	2.5	3.2	2.7	2.3
Core	4.2	3.2	2.2	3.2	2.7	2.5	2.4	4.0	3.2	2.5
Employment Cost Index	4.8	3.7	3.2	3.4	2.7	2.9	3.0	4.2	3.8	2.9
Unemployment Rate (%, sa)	3.8	4.0	4.2	4.3	4.5	4.5	4.4	-	-	-

* Q4/Q4 change

Source: J.P. Morgan

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Financial markets forecast

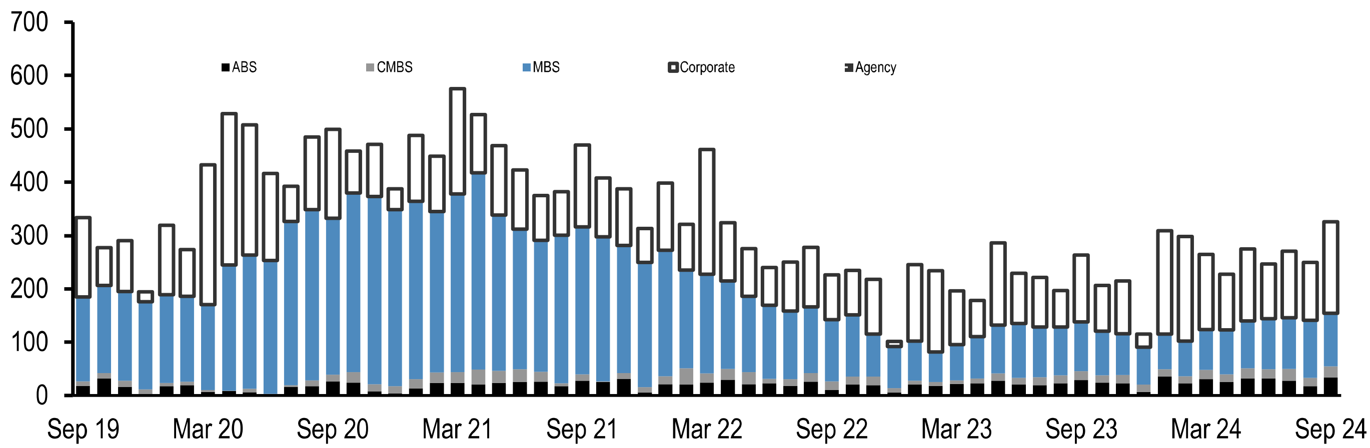
Credit Spread	Current	YE24
10-year SOFR swap spread (bp)	-49	-37
FNMA 30yr 6% Front Tsy OAS (bp)	34	30
10yr conduit CMBS LCF AAA	88	95
3-year AAA card ABS to Treasuries (bp)	44	40
JULI spread to Treasuries (bp)	92	110
High Yield Index	313	375
Emerging Market Index	337	400
Local currency: GBI-EM yield (%)	6.38%	5.58%

cont.

	Current	YE24
S&P 500 (level)	5973	4200
Brent ($/bbl)	75	83
Gold ($/oz)	2707	2281
EUR/USD	1.08	1.05
USD/JPY	153	149.5

Source: J.P. Morgan

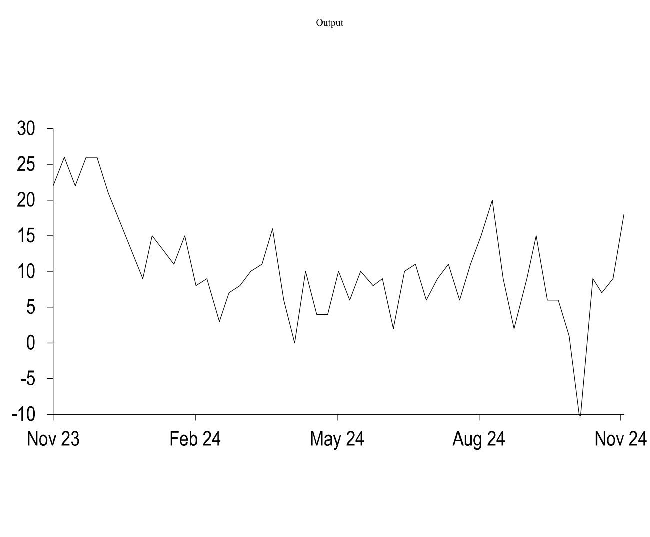
Gross fixed-rate product supply*



Treasury client survey

All Clients

	Long	Neutral	Short	Changes	Net longs
Nov 4, 2024	**24**	**70**	**6**	**17**	**18**
Oct 28, 2024	20	69	11	6	9
Oct 21, 2024	22	63	15	13	7
4-week avg	22	67	11		
52-week avg	21	69	10		



Source: J.P. Morgan

Source: J.P. Morgan

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Treasury net issuance forecast

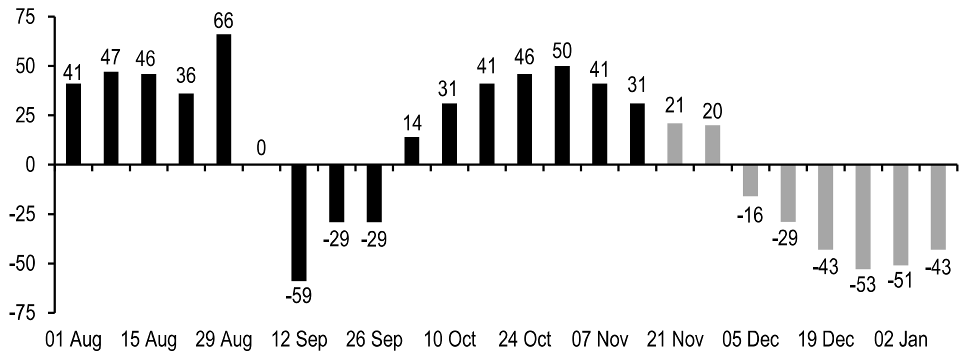
J.P. Morgan projection of net Treasury issuance to private investors, Federal Reserve purchases of Treasuries, and expected change in Treasuries held by private investors; $bn

Year	Net privately-held borrowing		Fed secondary market purchases		Net change in privately-held debt	
	Bills	Coupons	Bills	Coupons	Bills	Coupons
CY 2019	77	1133	169	77	-92	1056
CY 2020	2547	1752	157	2184	2390	-432
CY 2021	-1195	2898	0	957	-1195	1942
CY 2022	-37	1638	0	75	-37	1563
CY 2023	2047	1107	0	0	2047	1107
CY 2024	409	1922	0	0	409	1922

Source: J.P. Morgan, US Treasury, Federal Reserve Bank of New York

T-bill weekly net issuance

Weekly net issuance of T-bills, historical and JPM projections; $bn



Source: J.P. Morgan

Dealer inventories

Primary dealer positions in Treasuries*, with 5-year statistics; $bn

Maturity	Last	1w chg	5y avg	5y min	5y max	5y z-score
T-bills	37	-10	55	-4	119	-0.7
<2y	24	10	31	-17	96	-0.3
2-3y	18	5	5	-14	18	2.1
3-6y	63	0	31	-2	78	1.7
6-7y	17	1	13	-4	29	0.7
7-11y	26	-1	5	-10	35	2.2
>11y	48	0	47	27	62	0.3
11-21y	22	0				
>21y	27	0				
TIPS	18	-1	13	1	25	0.8
FRNS	14	6	7	-14	29	0.8
Total	264	10	207	76	361	0.9

Source: Federal Reserve Board of New York
*Latest data as of 10/30/2024

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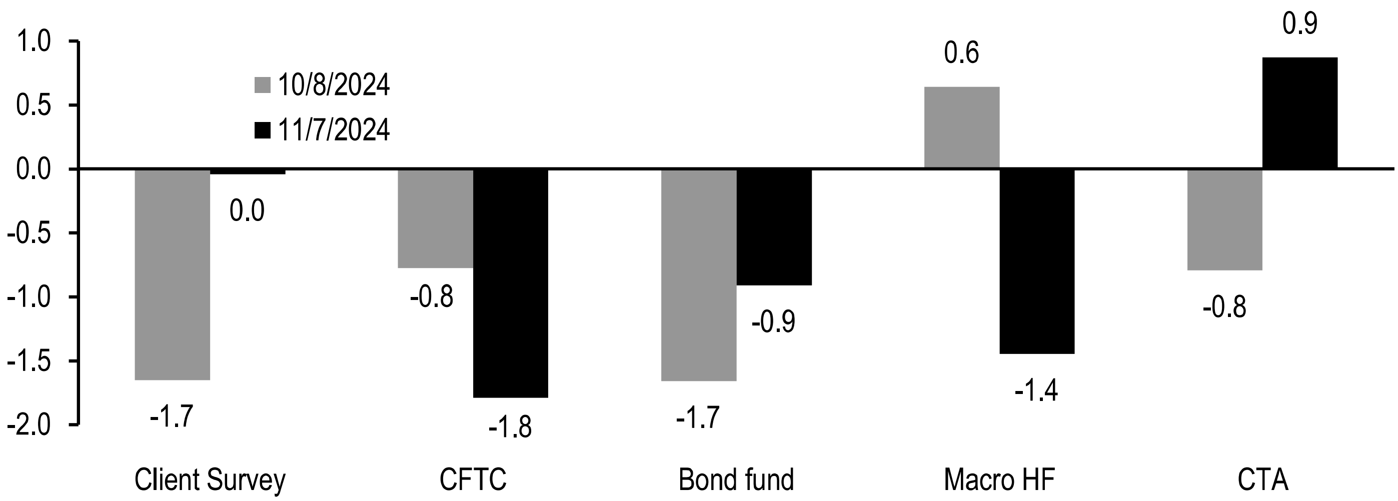
Investor position technical indicators

Current value of various position indicators* versus 1 month ago; 1-year z-score



Source: CFTC, Bloomberg Finance L.P, SG, HFR, J.P. Morgan
* JPM Client Survey refers to a 4-week moving average of our Treasury Client Survey Index; (Longs+Neutrals)/(Shorts+Neutrals), see *Survey Says: Using the Treasury Client Survey to predict rates moves*, 7/21/23for more details. CFTC refers to the non-commercial net longs in UST and SOFR futures contracts reported by the CFTC. CTA beta is the four-week partial beta of SG CTA Index to 10-year UST yields. Real money beta is the eight-week partial beta of excess returns of the 20 largest actively managed US core bond funds to 10-year UST yields. Macro HF beta is the six-week partial beta of HFRX Macro/CTA Index to 10-year UST yields

Treasury market functioning metrics

Various metrics of Treasury market functioning; units as indicated

Indicator	Today	1w chg	1y avg	1y min	1y max	1y z-score
Duration weighted mkt depth*; $mn	185	-81.2	234	94	346	-1.1
10y price impact**; 32nds	0.8	0.1	0.7	0.4	1.1	0.7
1m GC/OIS; bp	0.0	-16.6	9	0.0	32.2	-1.6
UST curve RMSE***; bp	1.3	0.0	1.4	0.0	1.7	-0.2
10s/3x old 10s ASW; bp	-0.4	-1.2	-0.5	-3.1	1.3	0.1
30s/3x old 30s ASW; bp	-0.2	-1.2	-0.2	-2.1	1.8	0.0

Source: J.P. Morgan, BrokerTec
* Market depth is the sum of the three bids and offers by queue position, averaged between 8:30 and 10:30am daily
** Price impact defined as the average move in order book mid-price against a $100mn flow in traded notional. See *Drivers of price impact and the role of hidden liquidity*, J. Younger et al., 1/13/17 for more details.
*** Root Mean Square Error of J.P. Morgan par fitted Treasury curve (see The (par) curves they are a-changin', 7/23/24)

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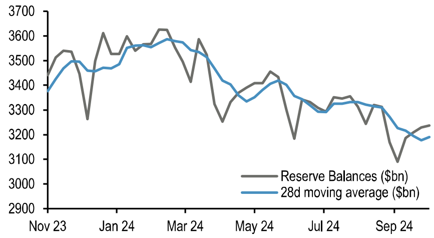
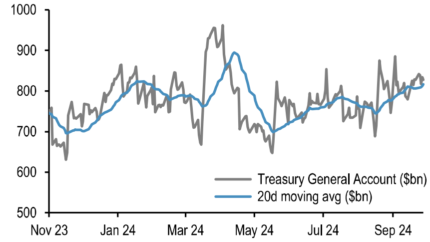
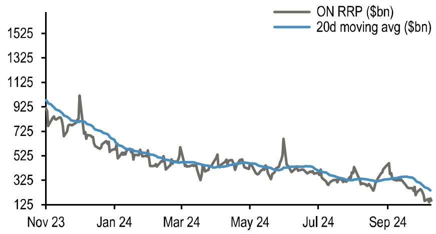
Select Federal Reserve balance sheet items







Select FRB Balance Sheet Items ($bn)	11/6/24	10/30/24	10/9/24	11/8/23	1wk Δ	1m Δ	1y Δ	1y avg	1y min	1y max	Percentile	Status**
Assets												
SOMA Holdings	6491	6509	6531	7225	-18	-40	-734	6812	6491	7225	0%	Narrow
T-bills	195	195	195	231	0	0	-36	204	195	231	23%	Narrow
Treasury Notes and Bonds	3680	3699	3701	4151	-19	-22	-472	3876	3680	4151	37%	Normal
Treasury FRNs	6	6	6	12	0	0	-5	8	5	12	51%	Normal
TIPS	341	341	344	365	0	-3	-24	353	341	366	6%	Narrow
Federal Agency Debt	2	2	2	2	0	0	0	2	2	2	0%	Narrow
Agency MBS	2258	2258	2274	2455	0	-16	-197	2360	2258	2455	0%	Narrow
Agency CMBS	8	8	8	8	0	0	0	8	8	8	0%	Narrow
Total Assets	6994	7013	7047	7861	-19	-53	-866	7388	6994	7861	0%	Narrow
Discount Window Borrowings	2	2	2	2	0	0	-1	4	1	9	9%	Narrow
Liabilities												
Reserves	3274	3237	3186	3329	37	88	-55	3395	3090	3626	21%	Narrow
Treasury General Account	840	847	820	793	-7	20	47	776	631	962	88%	Wide
Overnight RRP*	159	245	343	1024	-86	-184	-865	492	144	1033	1%	Narrow
Foreign RRP	395	398	396	319	-3	-1	76	371	319	420	72%	Wide
Other Deposits	159	155	154	160	4	5	-1	157	145	183	70%	Normal

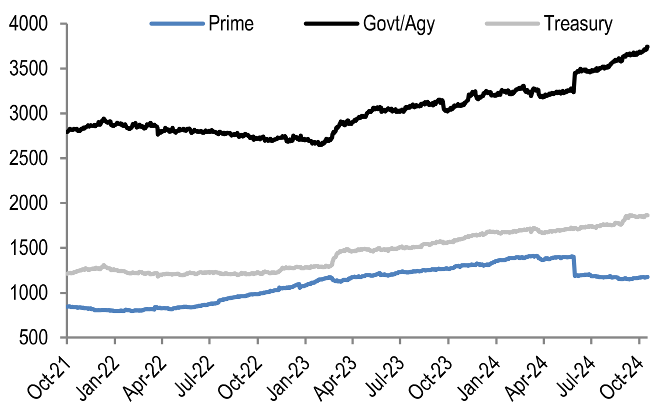
Source: Federal Reserve Bank, Bloomberg Finance L.P., J.P.Morgan

* Overnight RRP as of 11/07/24

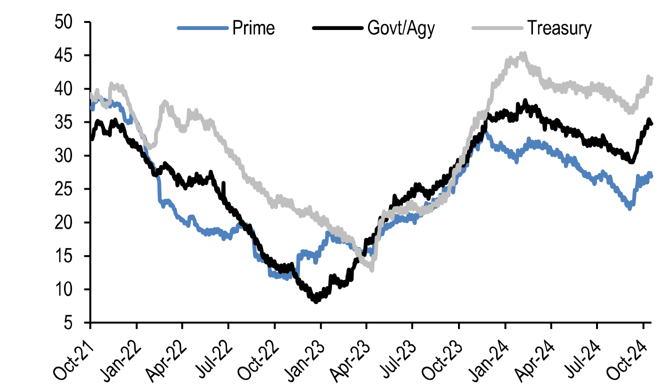
** Status: "Normal" means the current value is within 30-70% percentile over the past year. "Narrow" means the current value is within 10-30% percentile over the past year. "Wide" means the current value is within 70-90% percentile over the past year. A orange highlighted "Narrow" means the current value is less than 10% percentile over the past year. A orange highlighted "Wide" means the current value is greater than 90% percentile over the past year.

Money market funds

Assets under management ($bn)



Weighted average maturity (days)



Source: Crane Data, J.P. Morgan

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US funds flows

US Fund Flows ($mn)	Monthly Sep	Aug	Jul	Jun	May	Weekly 11/6/2024	10/30/2024	10/23/2024	10/16/2024	10/9/2024
UST	(161)	15,870	12,881	9,805	10,029	3,694	2,532	(328)	3,579	2,866
Mutual	(2,495)	341	(57)	572	698	556	62	(111)	(282)	(22)
ETF	2,334	15,529	12,939	9,233	9,331	3,139	2,470	(217)	3,861	2,888
IG	38,103	34,954	26,579	29,272	22,092	2,652	2,596	2,152	4,150	2,558
Mutual	18,286	17,332	8,008	(2,598)	11,794	2,756	872	1,376	1,529	1,502
ETF	19,817	17,622	18,571	31,870	10,298	663	3,283	1,523	3,482	1,757
HY	5,007	2,939	7,487	1,299	7,554	105	676	191	953	(301)
Mutual	2,902	2,270	4,528	(447)	2,450	354	97	508	53	707
ETF	2,105	669	2,960	1,746	5,104	(249)	579	(317)	901	(1,008)
LL	777	(4,232)	1,348	375	4,138	1,449	600	816	1,245	1,397
Mutual	(300)	(1,655)	198	126	2,283	371	206	182	73	403
ETF	1,078	(2,577)	1,149	249	1,855	1,078	394	634	1,172	993
Municipal	7,079	5,982	5,496	240	2,039	493	1,965	591	1,960	1,083
Mutual	5,460	4,374	2,245	(607)	1,110	(196)	447	595	758	1,159
ETF	1,619	1,608	3,252	846	928	689	1,518	(4)	1,202	(76)
Inflation Protected	124	489	(331)	(1,168)	(1,162)	(387)	436	(146)	74	(510)
Mutual	596	693	(415)	(782)	(1,052)	(39)	46	57	42	(46)
ETF	(472)	(204)	84	(386)	(109)	(348)	390	(203)	33	(463)
MBS	2,124	1,284	3,777	2,993	2,716	470	879	570	448	505
Mutual	679	547	432	750	73	374	127	111	230	335
ETF	1,446	737	3,345	2,243	2,644	96	752	459	218	170
Agg	17,491	15,153	12,730	24,568	13,342	8,842	7,375	4,529	5,965	5,731
Mutual	8,321	7,197	5,610	(1,592)	8,481	5,774	1,139	1,542	2,518	2,928
ETF	6,381	2,459	1,412	934	979	3,068	6,236	2,987	3,447	2,803
Equities	39,894	22,697	47,114	23,090	33,452	32,752	4,473	6,144	23,916	2,694
Mutual	(7,891)	(21,645)	(39,467)	(19,898)	(24,860)	(8,570)	(5,807)	(5,032)	(5,609)	(3,184)
ETF	47,785	44,342	86,581	42,988	58,313	41,322	10,281	11,176	29,526	5,878
MMFs	148,924	108,465	16,923	19,146	86,923	62,368	11,136	44,044	(15,417)	15,786
Prime	(16,678)	(10,980)	(11,167)	(207,917)	22,105	967	4,231	8,333	2,856	9,230
Government	165,602	119,445	28,090	227,063	64,818	61,401	6,905	35,711	(18,273)	6,556

Source: EPFR, Crane Data, J.P. Morgan

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Market Movers Calendar

Monday	Tuesday	Wednesday	Thursday	Friday
4 Nov **Factory orders**(10:00am) Oct Auction 3-year note $58bn	**5 Nov** **International trade**(8:30am) Sep -$84.5bn **ISM services**(10:00am) Oct 55.0 Auction 10-year note $42bn	**6 Nov** **Services PMI**(9:45am) Oct final 55.3 Auction 30-year bond $25bn	**7 Nov** **Productivity and costs prelim**(8:30am) 3Q 3.1% (1.7%oya) Unit labor costs 1.5% (3.6%oya) **Initial claims**(8:30am) w/e Nov 2 215,000 **Wholesale trade final**(10:00am) Sep **FOMC meeting**(2:00pm) Nov **Consumer credit**(3:00pm) Sep	**8 Nov** **Consumer sentiment**(10:00am) Nov prelim 71.0 Fed Governor Bowman speaks(11:00am)
11 Nov **Veterans Day, bond market closed**	**12 Nov** **NFIB survey**(6:00am) Oct **Senior loan officer survey**(2:00pm) 4Q Fed Governor Waller speaks(10:00am) Philadelphia Fed President Harker speaks(5:00pm)	**13 Nov** **CPI**(8:30am) Oct **Federal budget**(2:00pm) Oct Dallas Fed President Logan speaks(9:45am) Kansas City Fed President Schmid speaks(1:30pm)	**14 Nov** **PPI**(8:30am) Oct **Initial claims**(8:30am) w/e Nov 9 Announce 10-year TIPS (r) $17bn Announce 20-year bond $16bn Fed Chair Powell speaks(3:00pm) New York Fed President Williams speaks(4:15pm)	**15 Nov** **Retail sales**(8:30am) Oct **Import prices**(8:30am) Oct **Empire State survey**(8:30am) Nov **Industrial production**(9:15am) Oct **Business inventories**(10:00am) Sep
18 Nov **Business leaders survey**(8:30am) Nov **NAHB survey**(10:00am) Nov **TIC data**(4:00pm) Sep	**19 Nov** **Housing starts**(8:30am) Oct	**20 Nov** Auction 20-year bond $16bn	**21 Nov** **Initial claims**(8:30am) w/e Nov 16 **Philadelphia Fed manufacturing**(8:30am) Nov **Existing home sales**(10:00am) Oct **Leading indicators**(10:00am) Oct **QSS**(10:00am) 3Q adv **KC Fed survey**(11:00am) Nov Auction 10-year TIPS (r) $17bn Announce 2-year note $69bn Announce 2-year FRN (r) $28bn Announce 7-year note $44bn Announce 5-year note $70bn	**22 Nov** **Manufacturing PMI**(9:45am) Nov flash **Services PMI**(9:45am) Nov flash **Consumer sentiment**(10:00am) Nov final
25 Nov **Dallas Fed manufacturing**(10:30am) Nov Auction 2-year note $69bn	**26 Nov** **Philadelphia Fed nonmanufacturing**(8:30am) Nov **FHFA HPI**(9:00am) Sep, 3Q **S&P/Case-Shiller HPI**(9:00am) Sep, 3Q **Richmond Fed survey**(10:00am) Nov **Consumer confidence**(10:00am) Nov **New home sales**(10:00am) Oct **Dallas Fed services**(10:30am) Nov Auction 2-year FRN (r) $28bn Auction 5-year note $70bn	**27 Nov** **Real GDP**(8:30am) 3Q second **Durable goods**(8:30am) Oct **Personal income**(8:30am) Oct **Advance economic indicators**(8:30am) Sep **Initial claims**(8:30am) w/e Nov 23 **Pending home sales**(10:00am) Oct Auction 7-year note $44bn	**28 Nov** **Thanksgiving Day, markets closed**	**29 Nov**

Source: Private and public agencies and J.P. Morgan. Further details available upon request.

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