

US strategy

US–Iran tensions heighten economic uncertainty; FOMC more cautious on rate-cut path

Key message

1. The FOMC kept the federal funds rate unchanged, in line with market expectations, and the dot plot still indicates one rate cut in each of 2026 and 2027. However, both the upward shift in the distribution of dots and Chair Powell’s post-meeting comments indicate that the threshold for future rate cuts will be elevated, implying a more cautious policy approach ahead.
2. The Fed’s official economic projections revised up the outlook for future economic growth and inflation, while only slightly raising the unemployment rate forecast for 2027F. However, the Summary of Economic Projections (SEP) indicates that the Fed perceives greater uncertainty for the economy at present.
3. At the post-meeting statement, Chair Powell described the current policy rate range as being at the “upper end of neutral” or “somewhat restrictive.” He also noted, “some participants discussed the possibility of a rate hike, though it was not the baseline view of most policymakers,” and reiterated that “if inflation fails to make further progress, rate cuts will not be appropriate.”
4. Although geopolitical risks in the Middle East add uncertainty, inflation is expected to ease in 2H26F as energy-related pressures subside. Should downside risks to the labor market materialize, rate-cut expectations may strengthen. We advise buying medium- and long-term Treasuries on yield spikes for short-term trading purposes, and taking profits once yields begin to decline in 3Q26F. We do not recommend long-term strategic positions at this point.

Event

At the March FOMC meeting, the committee kept the federal funds rate unchanged at 3.50–3.75%, in line with market expectations. Although the dot plot maintained guidance for one rate cut in each of 2026 and 2027, the upward shift in the distribution of dots and Chair Powell’s post-meeting comments indicate that the threshold for future rate cuts will be high and that policy decisions will be more cautious going forward. In addition, the recent US–Iran conflict has added uncertainty to the economic outlook, and the Fed is monitoring its impact on inflation expectations and price dynamics.

Analysis

The Fed’s FOMC meeting released updated projections on future economic data and interest rates (Figure 1), with the following key points:

1. Growth forecasts for 2026-28 and the long-run, revised upward to 2.4%, 2.3%, 2.1%, and 2.0%, respectively, reflecting resilience in US economic activity and improving productivity.
2. The unemployment rate forecast saw only a minor adjustment, with the 2027 estimate revised slightly from 4.2% to 4.3%. In contrast, inflation projections were revised higher. The 2026 PCE inflation forecast was raised from 2.4% to 2.7%, and core PCE from 2.5% to 2.7%. The 2027 PCE and core PCE forecasts were both nudged up to 2.2%, reflecting the impact of higher energy prices and slower progress on inflation.
3. The median policy rate projections in the dot plot were unchanged from December (Figure 2), indicating one rate cut in each of 2026 and 2027. However, the overall distribution of dots shifted slightly higher, and the long-run median rate was raised by 10bps, signaling that the higher-for-longer rate environment may persist.

The post-meeting statement featured only two meaningful adjustments: the labor market description was revised from “showing signs of stabilizing” to “little changed in recent months,” and a new sentence was added noting, “the implications of developments in the Middle East for the US economy are uncertain.” Beyond these items, the statement was largely unchanged. The Fed held the federal funds rate at 3.50–3.75%, as expected. However, Governor Stephen Miran dissented, favoring a 25bp rate cut.

During the press conference, Chair Powell described the current policy rate range as being at the “upper end of neutral” or “somewhat restrictive.” He also noted that “some participants discussed the possibility of a rate hike, though it was not the baseline view of most policymakers,” and reiterated that “if inflation fails to make further progress, rate cuts will not be appropriate.”, underscoring a higher threshold for future easing. When asked about the Fed’s response to rising energy prices, Powell said it was too early to assess given the elevated uncertainty, and stressed that the Fed will continue to monitor inflation expectations and other price indicators. The Summary of Economic Projections (SEP) likewise suggests that Fed officials perceive greater uncertainty for the economy at present (Figure 3).

Although the meeting did not include comments on Reserve Management Purchases (RMPs) or recent risk-taking by private credit, data from the New York Fed's System Open Market Account (SOMA) show that since RMPs were launched in December to bolster market liquidity, the Fed has conducted roughly US\$130bn in purchases. These operations are expected to raise the US banking system's reserves-to-nominal-GDP ratio back above 10%, indicating a more comfortable liquidity backdrop (Figure 4). However, current execution has already reached 60% of the program's first-year planned total of US\$220bn. If the overall program size is unchanged, monthly RMP purchase volumes are expected to taper off, and the associated liquidity impact on markets is likely to diminish.

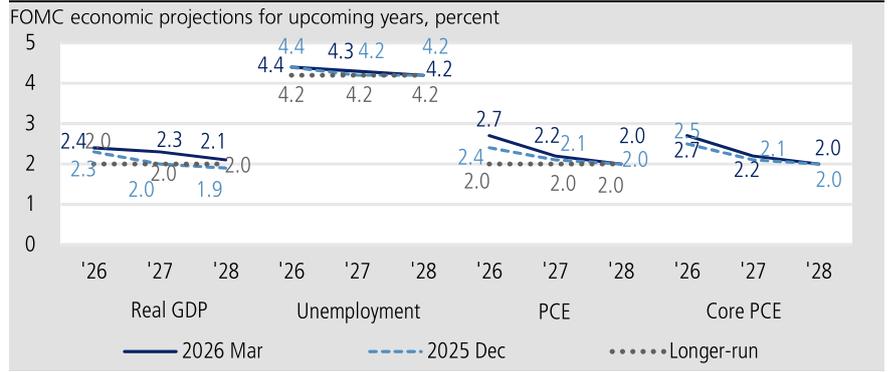
Market response & investment recommendations

Ahead of the FOMC meeting, renewed conflict in the Middle East pushed oil prices higher, pressuring risk assets, driving US Treasury yields upward, and strengthening the US dollar. Treasury yields initially pulled back following the release of the dot plot, which continued to signal 25bps of rate cuts in both 2026 and 2027. However, Chair Powell's post-meeting comments conveyed heightened caution toward rate cuts and a higher bar for policy easing. This tempered market expectations for rate cuts, sending Treasury yields and the US dollar higher, while equities and other risk assets extended their declines. Precious metals, including gold, also saw deeper pullbacks.

Although rising oil prices pose a meaningful risk to inflation, energy prices primarily affect headline inflation. If the US–Iran conflict concludes, and oil price shocks do not spill over into broader price categories, the impact on core inflation—the Fed's primary focus—should be limited. Historically, the Fed has often adopted a “wait-and-see” approach under similar circumstances. For example, during the oil surge triggered by the Arab Spring in 2011, then-Chair Bernanke viewed the spike as transitory. Likewise, the sharp rise in oil prices following the onset of the Russia–Ukraine conflict in 2022 did not prompt immediate aggressive tightening until inflation had clearly broadened into core goods and services. We believe this time will be no different, and that during this early stage of the US–Iran conflict, the Fed is likely to maintain a wait-and-see stance. However, if inflation expectations beyond two years become unanchored (Figure 5), or if energy-driven price pressures spill into core components, the Fed may find it difficult to avoid intervening.

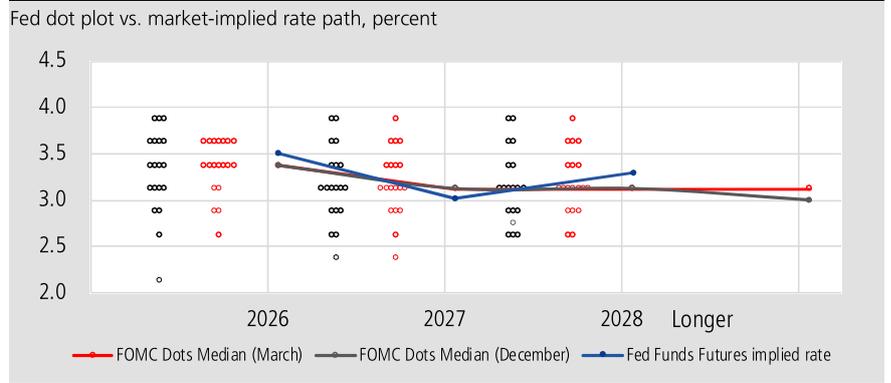
While Middle East conflict may keep oil prices elevated in the near term, our base case assumes an eventual cessation of the US–Iran conflict and a pullback in oil prices over the medium- and long term. Alongside the diminishing impact of tariff-related price pressures and a soft housing market suppressing shelter inflation, we expect inflation to trend lower in 2H26F. The deceleration in the US labor market will also cap wage and core services inflation. Over the past six months, both nonfarm payroll growth and job opening rates have declined noticeably, pointing to weakening labor demand. Excluding the healthcare and education sectors, which are less sensitive to the economic cycle, nonfarm payrolls, excluding healthcare and education, have shrank for five consecutive months (Figure 6), indicating that labor market conditions are less robust than headline data suggest, and remain uneven across sectors. As a result, the unemployment rate still faces upward pressure. We expect inflation to ease in 2H26F as the energy shock subsides. Should labor market downside risks materialize, the Fed may gain additional room to signal rate cuts. As such, we maintain our outlook for 25-50bps of rate cuts in the US this year. We recommend going long on medium- to long-duration US Treasuries in 2Q26F when yields spike for tactical trading purposes, and taking profits after rate cuts begin in 3Q26F. We do not recommend long-term strategic positioning at this point.

Figure 1: The Fed raised GDP forecasts for 2026-28; the 2026 PCE inflation forecast was raised to 2.7%, while the unemployment rate forecast held at 4.4%



Source: Fed; Bloomberg; KGI Research

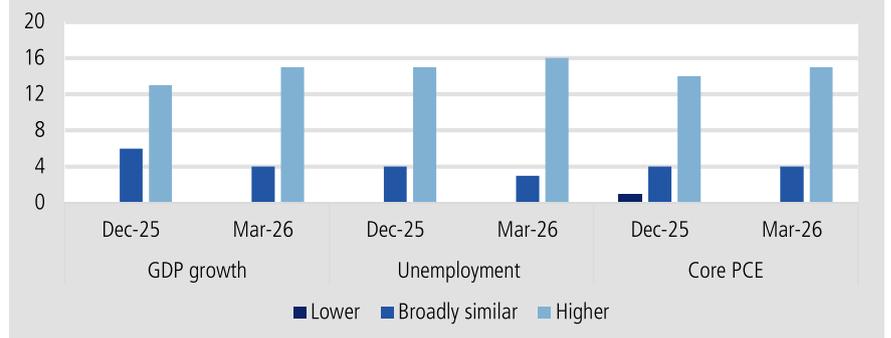
Figure 2: The March FOMC dot plot still indicates 25bps of rate cuts in each of 2026 & 2027



Source: Fed; Bloomberg; KGI Research

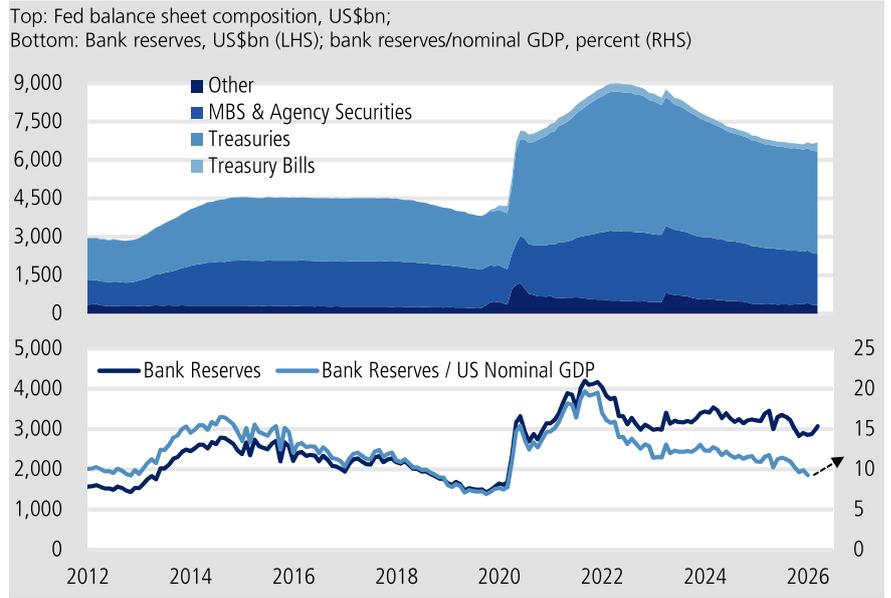
Figure 3: FOMC officials see higher uncertainty in the economic outlook

Number of participants assessing uncertainty in economic growth, unemployment & core PCE as lower/ unchanged/ higher in December 2025 vs. March 2026 meetings, count



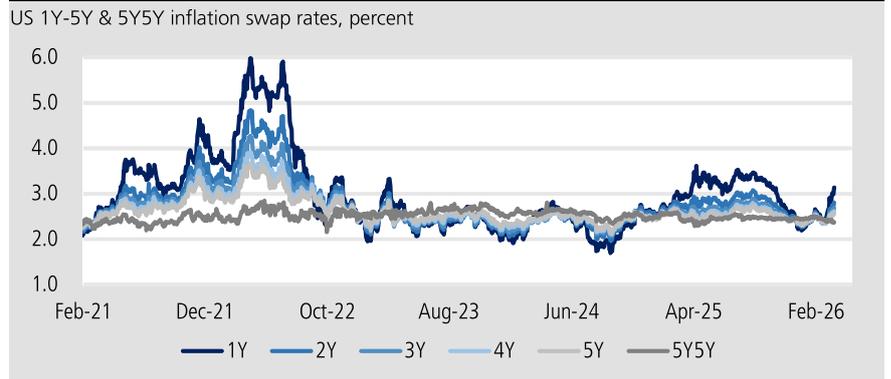
Source: Fed; Bloomberg; KGI Research

Figure 4: Since December 2025, the Fed has launched RMPs to continue purchasing T-bills and short-term Treasuries, lifting the US banking system's reserves-to-nominal-GDP ratio back above 10%



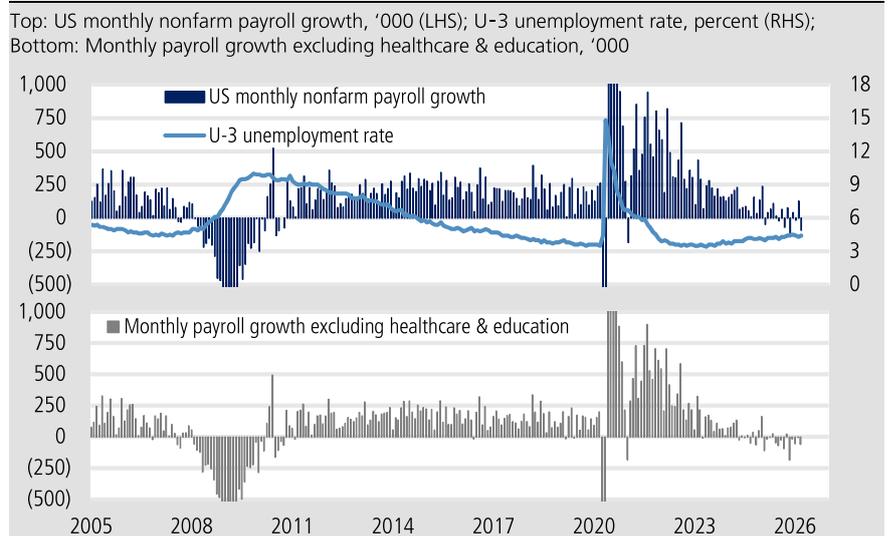
Source: Fed; Bloomberg; KGI Research

Figure 5: Inflation expectations will be a key indicator for the Fed in assessing inflation pressures



Source: Bloomberg; KGI Research

Figure 6: The US labor market is weaker than it appears; excluding healthcare & education, nonfarm payrolls have recorded negative growth for several months



Source: Bloomberg; KGI Research

Figure 7: Key US economic data

Indicators		Units	2021	2022	2023	2024	Mar-25	Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25	Jan-26	Feb-26	
GDP	GDP QoQ SAAR	QoQ % SAAR					(0.6)			3.8			4.4			1.4			
	GDP YoY	YoY %	6.2	2.5	2.9	2.8	2.0			2.1			2.3			2.2			
Consumer prices	CPI	YoY %	4.7	8.0	4.1	3.0	2.4	2.3	2.4	2.7	2.7	2.9	3.0		2.7	2.7	2.4	2.4	
	Core CPI	YoY %	3.6	6.2	4.8	3.4	2.8	2.8	2.8	2.9	3.1	3.1	3.0		2.6	2.6	2.5	2.5	
	PCE price index	YoY %	4.1	6.5	3.8	2.6	2.4	2.3	2.5	2.6	2.6	2.7	2.8	2.7	2.8	2.8	2.9		
	Core PCE index	YoY %	3.6	5.3	4.2	2.9	2.7	2.6	2.8	2.8	2.9	2.9	2.8	2.8	2.8	2.8	3.0		
Labor market	Labor force participation rate	%	62.0	62.3	62.5	62.5	62.5	62.6	62.4	62.3	62.2	62.3	62.5		62.5	62.4	62.1	62.0	
	Unemployment rate	%	5.4	3.6	3.6	4.0	4.2	4.2	4.3	4.1	4.3	4.3	4.4		4.5	4.4	4.3	4.4	
	Non farm payrolls	'000	7,268	4,526	2,515	1,459	67	108	13	(20)	64	(70)	76	(140)	41	(17)	126	(92)	
	Net Change In total employment in labor force	'000	6,078	4,526	2,515	1,459	171	389	(654)	83	(187)	230	286		232	(895)	(185)		
	Challenger job cut announce	YoY %	(1.2)	(1.7)	2.1	(0.9)	205	63	47	(2)	140	13	(26)	175	24	(8)	118	(72)	
	Opening/ hiring	x	1.56	1.75	1.58	1.43	1.33	1.32	1.41	1.40	1.38	1.41	1.43	1.39	1.35	1.24			
	Avg. hourly earnings	YoY %	4.9	4.9	4.1	4.1	4.2	3.9	4.0	3.9	4.0	4.0	4.0	3.8	3.9	3.9	3.7	3.7	3.8
Economic activity & business condition	Industrial production	YoY %	4.4	1.7	(0.2)	(0.7)	0.6	0.9	0.1	0.6	1.9	1.2	1.9	1.8	2.1	1.3	2.3		
	Durable goods orders	YoY %	18.4	8.8	3.7	(1.7)	9.8	2.6	17.5	12.6	3.6	5.1	9.7	4.6	10.5	12.6			
	Core capital goods orders	YoY %	13.4	8.6	(2.5)	(0.6)	2.2	0.5	2.2	4.5	4.4	2.5	5.3	6.2	4.1	7.9			
	Total business inventory/ sales ratio	x	1.29	1.36	1.41	1.40	1.38	1.38	1.39	1.38	1.37	1.37	1.37	1.38	1.37	1.36			
	Manufacturing inventory/ sales ratio	x	1.49	1.53	1.59	1.58	1.57	1.58	1.57	1.57	1.56	1.56	1.56	1.56	1.57	1.56			
	Retail inventory/ sales ratio	x	1.14	1.23	1.27	1.31	1.29	1.29	1.30	1.29	1.29	1.28	1.28	1.29	1.28	1.28			
	ISM manufacturing index	Point	60.6	53.5	47.1	48.2	48.9	48.8	48.6	49.0	48.4	48.9	48.9	48.8	48.0	47.9	52.6	52.4	
	ISM non-manufacturing index	Point	62.4	56.1	52.7	52.4	50.8	51.6	50.2	50.8	50.5	51.9	50.3	52.0	52.4	53.8	53.8	56.1	
	ISM manufacturing index: new orders	Point	64.3	51.6	46.0	48.7	45.6	47.5	48.3	46.9	47.5	51.1	48.7	48.7	47.3	47.4	57.1	55.8	
	Chicago Fed National activity Index	Point	0.37	(0.05)	(0.12)	(0.19)	0.16	(0.36)	(0.29)	(0.10)	0.00	(0.34)	(0.29)	(0.52)	(0.15)	(0.21)	0.18		
	Conference board leading index	YoY %	7.1	0.4	(7.5)	(4.8)	(3.6)	(4.3)	(3.9)	(4.0)	(3.5)	(3.5)	(3.3)	(3.3)	(3.8)	(3.9)			
	C&I Loans for large/medium - tightening lending standard	%	(15.1)	11.8	43.9	9.5		18.5			9.5			6.5			5.3		
	C&I Loans for large/medium - stronger demand	%	(1.2)	12.4	(42.3)	(18.2)		(20.3)			(28.6)			11.5			16.1		
Housing market	Building Permits	'000, SAAR	1,735	1,684	1,516	1,474	1,481	1,422	1,394	1,393	1,362	1,330	1,415	1,411	1,388	1,455	1,376		
	Housing starts	'000, SAAR	1,603	1,552	1,421	1,371	1,355	1,398	1,282	1,382	1,420	1,291	1,328	1,272	1,324	1,387	1,487		
	New home sales	'000, SAAR	769	637	665	685	660	706	627	662	639	706	719	656	758	745			
	Existing home sales	mn, SAAR	6.1	5.1	4.1	4.1	4.0	4.0	4.0	4.0	4.0	4.0	4.1	4.1	4.1	4.3	4.0	4.1	
	NAHB housing market index	Point, SA	81	59	44	45	39	40	34	32	33	32	32	37	38	39	37	36	
	S&P/Case-Shiller 20-city composite home price index	YoY %	18.7	4.9	6.5	4.6	4.1	3.4	2.8	2.1	1.8	1.6	1.4	1.4	1.4	1.4			
Consumption	Personal expenditures	YoY % SA	8.8	3.0	2.6	2.9	3.2	3.1	2.5	2.5	2.6	2.8	2.4	2.5	2.4	1.7			
	Retail sales	YoY %	18.1	9.1	3.5	2.6	5.1	5.0	3.4	4.4	4.1	5.0	4.1	3.2	3.2	2.4	3.2		
	Retail sales ex-autos	YoY %	17.2	10.6	3.3	2.8	4.2	4.1	3.7	4.0	4.0	4.8	3.8	3.7	4.1	3.3	3.9		
	Domestic vehicles sales	mn, SA	179.2	164.8	185.2	189.3	17.8	17.3	15.7	15.3	16.4	16.1	16.4	15.3	15.6	16.0	14.9	15.8	
	Conference board consumer confidence	Point	112.7	104.5	105.4	104.5	93.9	85.7	98.4	95.2	98.7	97.8	95.6	95.5	92.9	94.2	89.0	91.2	
Michigan Consumer Sentiment Index	Point	77.6	59.0	65.4	72.5	57.0	52.2	52.2	60.7	61.7	58.2	55.1	53.6	51.0	52.9	56.4	56.6		
Fiscal	Budget balance	As % of GDP	(10.4)	(5.3)	(6.3)	(6.9)	(7.0)	(6.8)	(6.7)	(6.3)	(6.4)	(6.2)	(5.8)	(5.9)	(5.3)	(5.4)	(5.3)	(5.2)	
Int'l balance	Current account balance	As % of GDP	(3.7)	(3.8)	(3.3)	(4.1)	(4.5)			(4.4)			(4.0)						
	Net foreign securities transactions	US \$bn	907	1,321	1,005	776	161.1	(24.0)	257.2	157.7	37.9	131.6	172.7	29.7	206.6	28.0			
Monetary & financial	Federal funds rate	%	0.25	4.50	5.50	4.50	4.50	4.50	4.50	4.50	4.50	4.50	4.25	4.00	4.00	3.75	3.75	3.75	
	10-Year treasury yield	%	1.51	3.87	3.88	4.57	4.21	4.16	4.40	4.23	4.37	4.23	4.15	4.08	4.01	4.17	4.24	3.94	
	Dollar index	Point	95.7	103.5	101.3	108.5	104.2	99.5	99.3	96.9	100.0	97.8	97.8	99.8	99.5	98.3	97.0	97.6	

Source: Bloomberg; KGI Research

Figure 8: Key Taiwan economic data

Indicators		Units	2021	2022	2023	2024	Mar-25	Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25	Jan-26	Feb-26
GDP	GDP YoY	YoY %	6.7	2.7	1.1	5.3	5.5	2.0	1.5	7.7			8.4			12.7		
Consumer prices	CPI	YoY %	2.0	3.0	2.5	2.2	2.3	1.5	1.4	1.5	1.6	1.3	1.5	1.2	1.3	0.7	1.8	
	Core CPI	YoY %	1.9	2.7	2.4	1.7	1.7	1.7	1.6	1.5	1.7	1.8	1.5	1.8	1.7	1.8	1.3	2.6
Labor market	Unemployment rate	%	3.7	3.6	3.4	3.4	3.4	3.4	3.3	3.4	3.3	3.3	3.4	3.3	3.4	3.4	3.4	
Economic activity	Industrial production	YoY %	14.7	(1.7)	(12.5)	11.6	14.1	25.4	24.6	20.6	20.1	15.2	18.2	15.9	18.4	23.1	28.5	
	Markit Taiwan manufacturing PMI	Point				50.9	49.8	47.8	48.6	47.2	46.2	47.4	46.8	47.7	48.8	50.9	51.7	55.2
	NDC monitoring light signal						Yellow-red	Yellow-red	Green	Green	Green	Green	Yellow-red	Yellow-red	Yellow-red	Red	Red	
	NDC monitoring indicators	Point	39.0	24.2	14.4	34.0	35.0	33.0	31.0	29.0	29.0	31.0	34.0	35.0	37.0	38.0	39.0	
	NDC composite leading index	YoY %	4.8	(3.2)	(1.6)	2.1	9.2	8.3	7.5	7.1	7.3	8.0	9.2	10.7	12.4	14.3	16.3	
	NDC composite coincident index	YoY %	8.7	(1.3)	(9.5)	3.4	15.0	15.8	16.2	16.3	16.5	16.9	17.5	18.3	18.9	19.4	19.7	
Consumption	Retail sales	YoY %	3.3	7.4	9.7	3.3	0.4	(0.6)	(1.4)	(2.9)	(3.6)	0.4	(1.6)	1.9	1.6	0.9	(3.5)	
Trade	Exports	US \$bn	446.6	479.7	432.6	475.3	49.5	48.7	51.7	53.3	56.7	58.4	54.2	60.9	64.1	62.5	65.8	49.8
	Imports	US \$bn	381.3	428.1	352.1	394.7	42.6	41.2	39.1	41.3	42.3	41.7	41.9	39.2	48.0	43.0	46.9	37.0
	Trade balance	US \$bn	65.3	51.6	80.5	80.6	6.9	7.4	12.6	12.1	14.4	16.8	12.4	21.7	16.1	19.4	18.9	12.8
	Export growth	YoY %	29.4	7.4	(9.8)	9.9	18.6	29.9	38.6	33.7	42.0	33.9	33.7	47.5	56.0	43.4	69.9	20.6
	Import growth	YoY %	33.4	12.3	(17.8)	12.1	28.7	32.9	24.8	17.2	20.4	29.5	25.1	14.5	44.9	14.9	63.6	6.8
	Export orders	US \$bn	674.1	666.8	561.0	589.6	54.9	59.1	60.8	59.8	60.5	60.1	70.3	69.4	73.0	76.2	76.9	
	Export order growth	YoY %	26.3	(1.1)	(15.9)	5.1	16.3	25.2	24.2	31.0	20.8	19.5	30.6	25.0	39.5	43.8	60.1	
Monetary & financial	M1B	YoY %	12.8	4.1	3.1	4.0	1.8	1.9	2.0	2.4	2.9	4.5	5.2	4.8	4.9	4.9	5.6	
	M2	YoY %	8.0	7.1	5.3	5.5	4.4	3.9	3.3	3.5	3.4	4.8	5.4	5.0	5.1	5.0	5.2	
	Foreign reserves	US \$bn	548.4	554.9	570.6	576.7	578.0	582.8	593.0	598.4	597.9	597.4	602.9	600.2	599.8	602.6	604.5	605.5
	Rediscount rate	%	1.1	1.8	1.9	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
	Exchange rate	USD/TWD	27.7	30.7	30.6	32.8	33.2	32.0	29.9	29.2	29.9	30.6	30.5	30.7	31.4	31.4	31.5	31.3

Source: Bloomberg; KGI Research

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