

US Economic Comment

FOMC 2015 Redux – September as "stage setter"

Economics

Americas

FOMC continues to expect a rate hike this year (think December)

"The Committee judges that the case for an increase...has strengthened but decided, for the time being, to wait for further evidence of continued progress toward its objectives." The committee also moved to a "roughly balanced" risk assessment, a move we had predicted after the July meeting; we wrote at that time that "the September FOMC could be used to reset expectations – noting that the risks are 'nearly balanced', implying a forthcoming rate hike" (see: [FOMC: Return of the Risk Statement](#)). The shift in the balance of risks, the waiting only "for the time being" in combination with a more positive assessment of the current economy, indicates a Fed rate hike later this year; we believe the most likely meeting for a move is December.

Lower dots bring Fed down to our 2017 forecast for rate hikes

In addition to the shift resulting from one fewer move in 2016, the median central tendency forecast by FOMC members also reduced the expected number of hikes in 2017 to only two rate hikes (in line with the UBS Economics policy rate forecast), lowering the projected year-end 2017 rate by 50bp. The median policy rate projections show an expected three rate hikes per year in 2017/18/19. They show a median terminal rate of between 2.75 and 3.00%, down from 3.0% previously.

Three dissents

Three FOMC members – Presidents George, Mester and Rosengren – dissented for a rate hike. The addition of President Rosengren, who had been more dovish up until his most recent speech (see: [Is September in play?](#)), is curious. We will watch other Fed speakers for the shift in tone we saw in his (and President Williams', a non-voter) speech. Despite these dissents, it is useful to note that three members of the FOMC saw no move likely in 2016.

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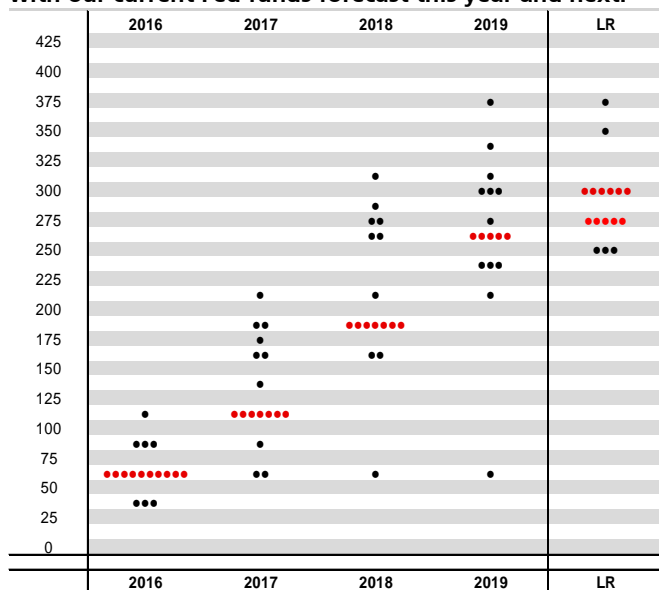
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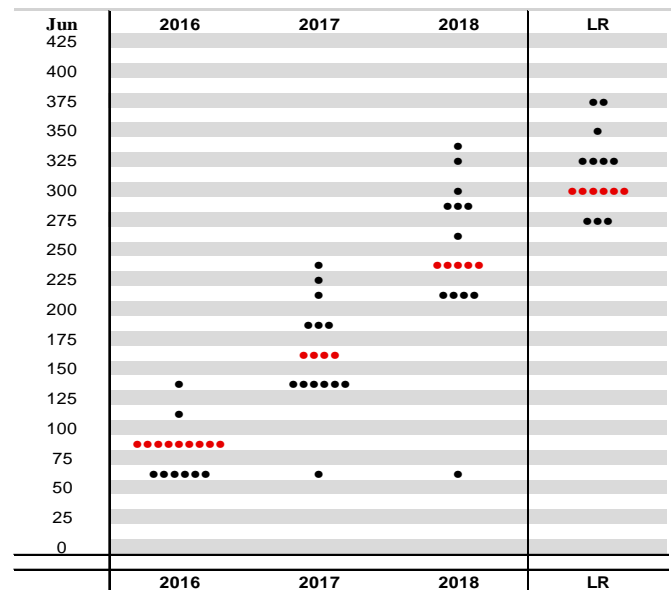
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Figure 1: The updated central tendency forecast is in line with our current Fed funds forecast this year and next.



Source: Federal Reserve and UBS Note: Red indicates median.

Figure 2: What the path looked like in June:



Source: Federal Reserve and UBS Note: Red indicates median.

Figure 3: September FOMC Statement versus July:

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Information received since the Federal Open Market Committee met in ~~June~~July indicates that the labor market ~~strengthened~~has continued to strengthen and that ~~growth of~~economic activity has been expanding at a moderate pace picked up from the modest pace seen in the first half of this year. ~~Although the unemployment rate. Job gains were strong in June following weak growth in May. On balance, payrolls and other labor market indicators point to some increase in labor utilization is little changed in recent months.~~ job gains have been solid, on average. Household spending has been growing strongly but business fixed investment has ~~been~~remained soft. Inflation has continued to run below the Committee's 2 percent longer-run objective, partly reflecting earlier declines in energy prices and in prices of non-energy imports. Market-based measures of inflation compensation remain low; most survey-based measures of longer-term inflation expectations are little changed, on balance, in recent months.

Consistent with its statutory mandate, the Committee seeks to foster maximum employment and price stability. The Committee ~~currently~~expects that, with gradual adjustments in the stance of monetary policy, economic activity will expand at a moderate pace and labor market ~~indicators~~conditions will strengthen ~~somewhat further~~inflation is expected to remain low in the near term, in part because of earlier declines in energy prices, but to rise to 2 percent over the medium term as the transitory effects of past declines in energy and import prices dissipate and the labor market strengthens further. Near-term risks to the economic outlook ~~have diminished~~appear roughly balanced. The Committee continues to closely monitor inflation indicators and global economic and financial developments.

Against this backdrop, the Committee decided to maintain the target range for the federal funds rate at 1/4 to 1/2 percent. The Committee judges that the case for an increase in the federal funds rate has strengthened but decided, for the time being, to wait for further evidence of continued progress toward its objectives. The stance of monetary policy remains accommodative, thereby supporting further improvement in labor market conditions and a return to 2 percent inflation.

In determining the timing and size of future adjustments to the target range for the federal funds rate, the Committee will assess realized and expected economic conditions relative to its objectives of maximum employment and 2 percent inflation. This assessment will take into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments. In light of the current shortfall of inflation from 2 percent, the Committee will carefully monitor actual and expected progress toward its inflation goal. The Committee expects that economic conditions will evolve in a manner that will warrant only gradual increases in the federal funds rate; the federal funds rate is likely to remain, for some time, below levels that are expected to prevail in the longer run. However, the actual path of the federal funds rate will depend on the economic outlook as informed by incoming data.

The Committee is maintaining its existing policy of reinvesting principal payments from its holdings of agency debt and agency mortgage-backed securities in agency mortgage-backed securities and of rolling over maturing Treasury securities at auction, and it anticipates doing so until normalization of the level of the federal funds rate is well under way. This policy, by keeping the Committee's holdings of longer-term securities at sizable levels, should help maintain accommodative financial conditions.

Voting for the FOMC monetary policy action were: Janet L. Yellen, Chair; William C. Dudley, Vice Chairman; Lael Brainard; James Bullard; Stanley Fischer; ~~Loretta J. Mester~~Eric Rosengren; Jerome H. Powell; ~~George~~and Daniel K. Tarullo. Voting against the action ~~was~~were Esther L. George, ~~who~~Loretta J. Mester, and Eric Rosengren, each of whom preferred at this meeting to raise the target range for the federal funds rate to 1/2 to 3/4 percent.

Source: Federal Reserve and UBS

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