Flash

Thursday, 28 April 2016

FOMC in no hurry to raise rates

- No policy change: FF target range remains 0.25-to-0.50%
- Fed drops phrase that global eco and fin. developments continue to pose risks
- FOMC continues to closely monitor inflation and global & fin. developments
- No trace of balanced risks to the outlook
- Kansas City Fed George dissents again in favour of 25 bps rate hike

No change in policy

The FOMC wasn't ready to give markets already more guidance about an eventual rate hike at the June meeting. The statement contained **only a few significant changes** when compared to the March statement. They are mentioned in the headlines. The disappearance of the phrase that "*global economic and financial developments continue to pose risks*" is crucial and means that the FOMC isn't worried anymore that these risks will have a crucial impact on the US economy and thus shouldn't play a main role in policymaking. Nevertheless, they reappeared in a much softer form further in the statement: *"The Committee continues to closely monitor inflation indicators and global economic and financial developments."* The underlined part was added at the meeting. So, new turmoil or substantial global economic weakness in the future may still have an impact on future policy.

The FOMC downgraded its assessment of the economic activity by stating that it *"appears to have slowed"*, but this was counterbalanced by a *"further improvement"* of labour market conditions. The growth downgrade was due to "*moderated growth in household spending*". The FOMC suggested though that an improvement was likely by adding "*households' real income has risen at solid pace and consumer sentiment remains high*".

Leaving out the phrase about the global economic and financial risks means that a rate hike is still possible in June, but the deterioration in domestic economic activity probably convinced the Fed not to stimulate market expectations about such move at the current juncture. In this respect, it was also important that the **FOMC didn't say anything about the balance of risks.** If the FOMC would have said that risks were balanced or nearly balanced, it would have signaled a higher likelihood of a Fed rate hike in June.

The data-dependent FOMC will now have two extra batches of monthly data and will monitor inflation and global economic and financial developments before it takes a decision at the June meeting, which remains a "live" meeting.

Markets relieved by "near" status quo

The probabilities of a rate hike were little changed at about 21% for June and 66% for the December meeting. US Treasuries gained some ground, following a string of 7 days of (modest) losses. The yield curve bull flattened with yields down between 6 (2-yr) and 10.7 bps (30yr) on a daily basis. Equities ended narrowly mixed with the S&P up 0.2%. EUR/USD was little changed, trading near 1.1320.

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