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Flash

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FOMC to tweak statement

No change of policy expected

Better financial conditions and Fed's projection of 2 hikes in 2016…

… could be enough to call risks to outlook balanced and open door for June hike

No change in policy

The FOMC concludes its two-day meeting Wednesday with a statement, but no press conference. Markets attach a 0% probability to a rate hike. Nobody expects a rate change and we have no reason at all to differ from the consensus. In the March Minutes, the FOMC de facto excluded an April move. *"..several (governors) expressed the view that a cautious approach to raising rates would be prudent or noted their concern that raising the target range as soon as April would signal a sense of urgency they did not think appropriate."*

Too little new info

Since the March meeting only one batch of eco data has been released. They have been generally weak and the outlook for Q1 growth, to be published Thursday, is awful. This justifies keeping rates unchanged. CPI Inflation dropped to 0.9% Y/Y in March from 1% Y/Y and 1.4% Y/Y in the previous two months. Average hourly earnings grew slowly and less than expected. Inflation expectations are fractionally higher. Those factors also support an unchanged outcome.

Financial conditions improved

In March, the Fed said that *"global economic and financial developments continue to pose risks."* Financial conditions improved and global economic indicators showed fragile signals of improvement. In this context, the FOMC may decide to keep the door open for a June rate increase. By that time, they'll have two extra batches of monthly economic data and may see more calm in financial markets. In March, the median Fed rate projections for 2016 was two hikes. The market discounts only a 19.6% chance for a rate hike in June and a 64.3% chance for December. That's still far away from the Fed's projected 2 rate increases of 25 bps. Some Fed governors, like even the dovish Rosengren, are a bit nervous about (low) market expectations.

Door for June hike will remain open

We believe that the Fed might tweak the statement to keep the option of a June rate hike open. In October, the Fed rather strongly suggested a December hike by referring to the next meeting as an important one to assess the progress made in fulfilling its dual mandate. **Now, it should be softer. The Fed's observation that risks to the outlook for both economic activity and the labour market are balanced, may re-appear.** Bringing that into the April statement could incite markets to discount more chances on a June rate hike, without making such a step highly likely. **Especially the Brexit-referendum, only days after the June meeting, might still intervene and convince the Fed to postpone a rate increase.** Of course, this factor shouldn't come up if the domestic economy doesn't revive, inflation (expectations) disappoint or if financial conditions worsen sharply. Such developments would as such be enough to postpone a rate hike.

Concluding, no rate change is expected. An attempt by the Fed to keep the door for a June hike (more) open and position the market in a more neutral way for such an outcome, is likely. It will be a mice step, but nevertheless a step towards an eventual rate hike. The impact on markets should be modest.

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