28 October 2015

FOMC meeting

Shifting to a tightening bias

- **The Fed shifted to a clear tightening bias and keeps December a 'live' FOMC meeting.**
- **Risks from abroad no longer a big concern.**
- **We place the highest odds on a January 2016 rate hike as manufacturing weakness is likely to keep Fed on hold in December.**

The Fed sent a clear message in its October FOMC statement: a hike at the December FOMC meeting is a real option and whether we will see the first rate hike in December or next year depends upon the data.

In its forward guidance the Fed is now flagging a clear tightening bias as its wording was changed to 'In determining whether it will be appropriate to RAISE the target range at its NEXT meeting...' from 'In determining HOW LONG to MAINTAIN this target range...'. The conditions remain unchanged 'when it has seen some further improvement in the labor market and is reasonably confident that inflation will move back to its 2 percent objective over the medium term.'

Further, the reference that 'Recent global economic and financial developments may restrain economic activity' was removed from the statement which now only says that the FOMC is 'monitoring' global financial and economic developments. Hence, the Fed's assessment is that risks from abroad have abated and there is one hurdle less towards a rate hike, in our view.

The statement acknowledges that the pace of job growth has slowed recently but repeats that underutilisation has diminished since early this year. Economic activity is described as 'has been' expanding at a moderate pace instead of 'is', which suggests that the Fed is not completely sure about the pace of growth right now and would like to see data that confirm the moderate pace of expansion in coming months.

We continue to place the highest odds on a January rate hike from the Fed as we believe that the weakness in the manufacturing sector will keep the Fed in a wait-and-see mode at the December meeting but that it will use the meeting to prepare markets for a near term rate hike.

Given the tightening bias in tonight's FOMC statement it seems fair that the market now attaches a higher probability, currently 45% compared to the pre meeting 32%, for a rate hike in December. A more firm pricing of a December rate hike, will require data confirming that the US economy is growing above potential. The next data releases to watch are the Q3 Employment Cost Index released on Friday and next week's October manufacturing ISM release and employment report.

Senior Analyst
Signe Roed-Frederiksen
+45 45128229
sroe@danskebank.dk

Important disclosures and certifications are contained from page 2 of this report.

Disclosures

This research report has been prepared by Danske Bank Markets, a division of Danske Bank A/S ('Danske Bank'). The author of the research report is Signe Roed-Frederiksen, Senior Analyst.

Analyst certification

Each research analyst responsible for the content of this research report certifies that the views expressed in the research report accurately reflect the research analyst's personal view about the financial instruments and issuers covered by the research report. Each responsible research analyst further certifies that no part of the compensation of the research analyst was, is or will be, directly or indirectly, related to the specific recommendations expressed in the research report.

Regulation

Danske Bank is authorised and subject to regulation by the Danish Financial Supervisory Authority and is subject to the rules and regulation of the relevant regulators in all other jurisdictions where it conducts business. Danske Bank is subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority (UK). Details on the extent of the regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available from Danske Bank on request.

The research reports of Danske Bank are prepared in accordance with the Danish Society of Financial Analysts' rules of ethics and the recommendations of the Danish Securities Dealers Association.

Conflicts of interest

Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high-quality research based on research objectivity and independence. These procedures are documented in Danske Bank's research policies. Employees within Danske Bank's Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and the Compliance Department. Danske Bank's Research Departments are organised independently from and do not report to other business areas within Danske Bank.

Research analysts are remunerated in part based on the overall profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.

Financial models and/or methodology used in this research report

Calculations and presentations in this research report are based on standard econometric tools and methodology as well as publicly available statistics for each individual security, issuer and/or country. Documentation can be obtained from the authors on request.

Risk warning

Major risks connected with recommendations or opinions in this research report, including a sensitivity analysis of relevant assumptions, are stated throughout the text.

Date of first publication

See the front page of this research report for the date of first publication.

General disclaimer

This research has been prepared by Danske Bank Markets (a division of Danske Bank A/S). It is provided for informational purposes only. It does not constitute or form part of, and shall under no circumstances be considered as, an offer to sell or a solicitation of an offer to purchase or sell any relevant financial instruments (i.e. financial instruments mentioned herein or other financial instruments of any issuer mentioned herein and/or options, warrants, rights or other interests with respect to any such financial instruments) ('Relevant Financial Instruments').

The research report has been prepared independently and solely on the basis of publicly available information that Danske Bank considers to be reliable. While reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation is made as to its accuracy or completeness and Danske Bank, its affiliates and subsidiaries accept no liability whatsoever for any direct or consequential loss, including without limitation any loss of profits, arising from reliance on this research report.

The opinions expressed herein are the opinions of the research analysts responsible for the research report and reflect their judgement as of the date hereof. These opinions are subject to change, and Danske Bank does not undertake to notify any recipient of this research report of any such change nor of any other changes related to the information provided in this research report.

This research report is not intended for retail customers in the United Kingdom or the United States.

This research report is protected by copyright and is intended solely for the designated addressee. It may not be reproduced or distributed, in whole or in part, by any recipient for any purpose without Danske Bank's prior written consent.

Disclaimer related to distribution in the United States

This research report is distributed in the United States by Danske Markets Inc., a U.S. registered broker-dealer and subsidiary of Danske Bank, pursuant to SEC Rule 15a-6 and related interpretations issued by the U.S. Securities and Exchange Commission. The research report is intended for distribution in the United States solely to 'U.S. institutional investors' as defined in SEC Rule 15a-6. Danske Markets Inc. accepts responsibility for this research report in connection with distribution in the United States solely to 'U.S. institutional investors'.

Danske Bank is not subject to U.S. rules with regard to the preparation of research reports and the independence of research analysts. In addition, the research analysts of Danske Bank who have prepared this research report are not registered or qualified as research analysts with the NYSE or FINRA but satisfy the applicable requirements of a non-U.S. jurisdiction.

Any U.S. investor recipient of this research report who wishes to purchase or sell any Relevant Financial Instrument may do so only by contacting Danske Markets Inc. directly and should be aware that investing in non-U.S. financial instruments may entail certain risks. Financial instruments of non-U.S. issuers may not be registered with the U.S. Securities and Exchange Commission and may not be subject to the reporting and auditing standards of the U.S. Securities and Exchange Commission.