

Essentials of the Monetary Policy

December 17, 2014



FEDERAL RESERVE

Patience...

ACCORDING TO THE FEDERAL RESERVE (Fed)

- The Committee decided to keep the target range for the federal funds rate at 0.00% to 0.25%.
- The Committee judges that it can be patient in beginning to normalize the stance of monetary policy. The Committee sees this guidance as consistent with its previous statement that it likely will be appropriate to maintain the 0 to ¼ percent target range for the federal funds rate for a considerable time following the end of its asset purchase program in October. However, if incoming information indicates faster progress toward the Committee's employment and inflation objectives than the Committee now expects, then increases in the target range for the federal funds rate are likely to occur sooner than currently anticipated. Conversely, if progress proves slower than expected, then increases in the target range are likely to occur later than currently anticipated.
- Information received since the Federal Open Market Committee met in October suggests that economic activity is expanding at a moderate pace. Labor market conditions improved further, with solid job gains and a lower unemployment rate. On balance, a range of labor market indicators suggests that underutilization of labor resources continues to diminish. Household spending is rising moderately and business fixed investment is advancing, while the recovery in the housing sector remains slow.
- Inflation has continued to run below the Committee's longer-run objective, partly reflecting declines in energy prices. Market-based measures of inflation compensation have declined somewhat further; survey-based measures of longer-term inflation expectations have remained stable.

COMMENTS

With all the recent movement in financial markets, particularly in oil prices, this meeting of the Fed was greatly anticipated. However, there is little that is new in the Fed's statement. While good economic data piles up in the United States and falling gas prices is largely seen as positive for U.S. growth, the Fed barely changed its view of conditions at all. It slightly revised upwards the forecast for real GDP growth in 2014, but the expectations remain the same for 2015. The jobless rate forecast for 2015 has been

lowered from between 5.4% and 5.6% to between 5.2% and 5.3%, which is within the Fed's long-term range.

The downward revision of inflation forecasts is larger. The range for the annual change in the consumer spending deflator forecast for the end of 2015 went from between 1.6% and 1.9% to between 1.0% and 1.6%. Even core inflation, which excludes food and energy, was revised downwards. Fed leaders therefore seem to be serving two masters with inflation: on the one hand, it is hoping that inflation will return to its 2% target, yet it must face the fact that oil prices will have a major impact on total inflation in the coming months. Our scenarios predict that the annual change in consumer prices will fall below 1% in the coming months.

Despite better economic growth, temporarily low inflation will prevent the Fed from committing to early movement by its key rates. It is therefore being patient, and this patience must be perceived as the equivalent of the previous forward guidance. Janet Yellen also specified that it was unlikely that the Fed would begin raising rates for at least the next couple of meetings. Fed leaders still predict several rate increases in 2015 even though the median for the key rate forecast for the end of next year was revised downwards, from 1.325% to 1.125%. Fed leaders now see four rate increases in 2015; this is in line with our own scenario.

Implications: The Fed is staying the course and the implications of its new forward guidance are not really different from what could have been concluded previously. Despite the foreseeable weakness in short-term inflation and certain measures of inflation expectations, improved economic conditions make it likely we will see a first increase in key rates in mid-2015.

Francis Généreux
Senior Economist

François Dupuis
Vice-President and Chief Economist

Mathieu D'Anjou
Senior Economist

Francis Généreux
Senior Economist

Jimmy Jean
Senior Economist

Hendrix Vachon
Senior Economist

514-281-2336 or 1 866 866-7000, ext. 2336
E-mail: desjardins.economics@desjardins.com

Schedule 2014 of Central Bank meetings

	<u>Decision</u>	<u>Rate</u>		<u>Decision</u>	<u>Rate</u>		
JANUARY			JULY				
9	European Central Bank	s.q.	0.25	1	Reserve Bank of Australia	s.q.	2.50
9	Bank of England	s.q.	0.50	3	European Central Bank	s.q.	0.15
15	Bank of Brazil	+50 b.p.	10.50	3	Bank of Sweden	-50 b.p.	0.25
21-22	Bank of Japan	---	---	10	Bank of England	s.q.	0.50
22	Bank of Canada	s.q.	1.00	11	Bank of Mexico	s.q.	3.00
29	Reserve Bank of New Zealand	s.q.	2.50	14-15	Bank of Japan	---	---
29	Federal Reserve	s.q.	0.25	16	Bank of Brazil	s.q.	11.00
31	Bank of Mexico	s.q.	3.50	16	Bank of Canada	s.q.	1.00
FEBRUARY			AUGUST				
3	Reserve Bank of Australia	s.q.	2.50	5	Reserve Bank of Australia	s.q.	2.50
6	European Central Bank	s.q.	0.25	7	European Central Bank	s.q.	0.15
6	Bank of England	s.q.	0.50	7	Bank of England	s.q.	0.50
13	Bank of Sweden	s.q.	0.75	7-8	Bank of Japan	---	---
17-18	Bank of Japan	---	---	SEPTEMBER			
26	Bank of Brazil	+25 b.p.	10.75	2	Reserve Bank of Australia	s.q.	2.50
MARCH			OCTOBER				
3	Reserve Bank of Australia	s.q.	2.50	2	European Central Bank	s.q.	0.05
5	Bank of Canada	s.q.	1.00	6	Reserve Bank of Australia	s.q.	2.50
6	European Central Bank	s.q.	0.25	6-7	Bank of Japan	---	---
6	Bank of England	s.q.	0.50	9	Bank of England	s.q.	0.50
10-11	Bank of Japan	---	---	22	Bank of Canada	s.q.	1.00
12	Reserve Bank of New Zealand	+25 b.p.	2.75	23	Bank of Norway	s.q.	1.50
19	Federal Reserve	s.q.	0.25	28	Bank of Sweden	-25 b.p.	0.00
20	Swiss National Bank	s.q.	0.00	29	Reserve Bank of New Zealand	s.q.	3.50
21	Bank of Mexico	s.q.	3.50	29	Bank of Brazil	+25 b.p.	11.25
27	Bank of Norway	s.q.	1.50	29	Federal Reserve	s.q.	0.25
31	Reserve Bank of Australia	s.q.	2.50	31	Bank of Japan	---	---
APRIL			NOVEMBER				
2	Bank of Brazil	+25 b.p.	11.00	3	Reserve Bank of Australia	s.q.	2.50
3	European Central Bank	s.q.	0.25	6	European Central Bank	s.q.	0.05
7-8	Bank of Japan	---	---	6	Bank of England	s.q.	0.50
9	Bank of Sweden	s.q.	0.75	18-19	Bank of Japan	---	---
10	Bank of England	s.q.	0.50	DECEMBER			
16	Bank of Canada	s.q.	1.00	1	Reserve Bank of Australia	s.q.	2.50
23	Reserve Bank of New Zealand	+25 b.p.	3.00	3	Bank of Brazil	+50 b.p.	11.75
25	Bank of Mexico	s.q.	3.50	3	Bank of Canada	s.q.	1.00
30	Bank of Japan	---	---	4	European Central Bank	s.q.	0.05
30	Federal Reserve	s.q.	0.25	4	Bank of England	s.q.	0.50
MAY			NOVEMBER				
6	Reserve Bank of Australia	s.q.	2.50	5	Bank of Mexico	s.q.	3.00
8	European Central Bank	s.q.	0.25	10	Reserve Bank of New Zealand	s.q.	3.50
8	Bank of England	s.q.	0.50	11	Bank of Norway	-25 b.p.	1.25
8	Bank of Norway	s.q.	1.50	11	Swiss National Bank	s.q.	0.00
20-21	Bank of Japan	---	---	16	Bank of Sweden	s.q.	0.00
28	Bank of Brazil	s.q.	11.00	17	Federal Reserve	s.q.	0.25
JUNE			NOVEMBER				
3	Reserve Bank of Australia	s.q.	2.50	18-19	Bank of Japan	---	---
4	Bank of Canada	s.q.	1.00	DECEMBER			
5	European Central Bank	-10 b.p.	0.15	1	Reserve Bank of Australia	s.q.	2.50
5	Bank of England	s.q.	0.50	3	Bank of Brazil	+50 b.p.	11.75
6	Bank of Mexico	-50 b.p.	3.00	3	Bank of Canada	s.q.	1.00
11	Reserve Bank of New Zealand	+25 b.p.	3.25	4	European Central Bank	s.q.	0.05
12-13	Bank of Japan	---	---	4	Bank of England	s.q.	0.50
18	Federal Reserve	s.q.	0.25	5	Bank of Mexico	s.q.	3.00
19	Bank of Norway	s.q.	1.50	10	Reserve Bank of New Zealand	s.q.	3.50
19	Swiss National Bank	s.q.	0.00	11	Bank of Norway	-25 b.p.	1.25
				11	Swiss National Bank	s.q.	0.00
				16	Bank of Sweden	s.q.	0.00
				17	Federal Reserve	s.q.	0.25
				18-19	Bank of Japan	---	---

NOTE: Certain banks may decide to change rates in-between the scheduled meetings. The abbreviations s.q. and b.p. correspond to status quo and basis points respectively.