



## FEDERAL RESERVE

### The (widely anticipated) end of an era

#### ACCORDING TO THE FEDERAL RESERVE (Fed)

- The Committee decided to raise the target range for the federal funds rate to 0.25% to 0.50%. The stance of monetary policy remains accommodative after this increase.
- The Committee expects that economic conditions will evolve in a manner that will warrant only gradual increases in the federal funds rate.
- Information received since the Federal Open Market Committee met in October suggests that economic activity has been expanding at a moderate pace. Household spending and business fixed investment have been increasing at solid rates in recent months, and the housing sector has improved further; however, net exports have been soft. A range of recent labor market indicators, including ongoing job gains and declining unemployment, shows further improvement and confirms that underutilization of labor resources has diminished appreciably since early this year.
- Inflation has continued to run below the Committee's 2% longer-run objective, partly reflecting declines in energy prices and in prices of non-energy imports. Market-based measures of inflation compensation remain low; some survey-based measures of longer-term inflation expectations have edged down.

#### COMMENTS

It was long awaited, this first U.S. key interest rate hike! In fact, this is the first increase since June 2006. Interest rates have been at floor level since the end of 2008, although this apparent stagnation hides the fact that the Fed has been very active with its quantitative policies. Nevertheless, today's decision marks the end of an era.

This rate hike symbolizes the beginning of a normalization process. Yet, the increase is a modest one: just 0.25%. Moreover, interest rates are still extremely low. The U.S. economy should easily cope with this start to monetary firming. Furthermore, the markets have been fully anticipating the Fed's decision, which had been broadly telegraphed in recent speeches by several leaders, including Janet Yellen.

The Fed states in its press release that interest rates will be raised very gradually, reminding us that the next moves will depend on the economic outlook. In this regard, the Fed's forecasts of real GDP growth, inflation and the unemployment rate have changed little from those that were issued in September. The expected annual change in real GDP for the fourth quarter of 2016 is 2.4%, versus the previous forecast of 2.3%.

As for the future rate hikes predicted by those attending the meeting, we note that the median is calling for four hikes of 0.25% in 2016 and four more in 2017. This would raise the top of the federal funds target range from 0.50%, after today's meeting, to 1.50% in December 2016 (the same forecast as in September). For the end of 2017, the median is expected to be 2.50%, slightly below what was anticipated in the previous exercise.

These forecasts show that the Fed hopes to distance itself from previous episodes of monetary firming. Readers will recall that between 2004 and 2006, every meeting ended with a 25 basis point hike. This time, the changes will not be so regular. But four rate hikes per year suggest a stop-and-go approach that could generate some volatility in the markets. In addition, economic developments, in particular problems in the manufacturing sector (with an ISM reading below the 50 mark) caused by a strong dollar, could result in rate hikes being even more incremental than the monetary policy committee members are predicting.

**Implications:** Today's rate hike is a first step towards the normalization of monetary policy, one that will be very gradual. For the years to come, the Fed appears to be contemplating rate increases of 25 basis points per quarter, but it is likely that any temporary deterioration in economic conditions will cause it to skip some of them.

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## Schedule 2015 of Central Bank meetings

	<u>Decision</u>	<u>Rate</u>		<u>Decision</u>	<u>Rate</u>
<b>JANUARY</b>					
8	Bank of England	s.q.	0.50		
14	Bank of Korea	s.q.	2.00		
15	Swiss National Bank	-50 b.p.	-0.75		
20-21	Bank of Japan	---	---		
21	Bank of Brazil	+50 b.p.	12.25		
21	Bank of Canada	-25 b.p.	0.75		
22	European Central Bank	s.q.	0.05		
28	Reserve Bank of New Zealand	s.q.	3.50		
28	Federal Reserve	s.q.	0.25		
29	Bank of Mexico	s.q.	3.00		
<b>FEBRUARY</b>					
2	Reserve Bank of Australia	-25 b.p.	2.25		
5	Bank of England	s.q.	0.50		
12	Bank of Sweden	-10 b.p.	-0.10		
16	Bank of Korea	s.q.	2.00		
17-18	Bank of Japan	---	---		
<b>MARCH</b>					
2	Reserve Bank of Australia	s.q.	2.25		
4	Bank of Brazil	+50 b.p.	12.75		
4	Bank of Canada	s.q.	0.75		
5	European Central Bank	s.q.	0.05		
5	Bank of England	s.q.	0.50		
11	Bank of Korea	-25 b.p.	1.75		
11	Reserve Bank of New Zealand	s.q.	3.50		
16-17	Bank of Japan	---	---		
18	Bank of Sweden	-15 b.p.	-0.25		
18	Federal Reserve	s.q.	0.25		
19	Bank of Norway	s.q.	1.25		
19	Swiss National Bank	s.q.	-0.75		
26	Bank of Mexico	s.q.	3.00		
<b>APRIL</b>					
7	Reserve Bank of Australia	s.q.	2.25		
7-8	Bank of Japan	---	---		
9	Bank of England	s.q.	0.50		
9	Bank of Korea	s.q.	1.75		
15	European Central Bank	s.q.	0.05		
15	Bank of Canada	s.q.	0.75		
29	Reserve Bank of New Zealand	s.q.	3.50		
29	Bank of Sweden	s.q.	-0.25		
29	Bank of Brazil	+50 b.p.	13.25		
29	Federal Reserve	s.q.	0.25		
30	Bank of Japan	---	---		
30	Bank of Mexico	s.q.	3.00		
<b>MAY</b>					
5	Reserve Bank of Australia	-25 b.p.	2.00		
7	Bank of Norway	s.q.	1.25		
11	Bank of England	s.q.	0.50		
15	Bank of Korea	s.q.	1.75		
21-22	Bank of Japan	---	---		
27	Bank of Canada	s.q.	0.75		
<b>JUNE</b>					
2	Reserve Bank of Australia	s.q.	2.00		
3	European Central Bank	s.q.	0.05		
3	Bank of Brazil	+50 b.p.	13.75		
4	Bank of England	s.q.	0.50		
4	Bank of Mexico	s.q.	3.00		
10	Bank of Korea	-25 b.p.	1.50		
10	Reserve Bank of New Zealand	-25 b.p.	3.25		
17	Federal Reserve	s.q.	0.25		
18	Bank of Norway	-25 b.p.	1.00		
18	Swiss National Bank	s.q.	-0.75		
18-19	Bank of Japan	---	---		
<b>JULY</b>					
2	Bank of Sweden	-10 b.p.	-0.35		
7	Reserve Bank of Australia	s.q.	2.00		
8	Bank of Korea	s.q.	1.50		
9	Bank of England	s.q.	0.50		
14-15	Bank of Japan	---	---		
15	Bank of Canada	-25 b.p.	0.50		
16	European Central Bank	s.q.	0.05		
22	Reserve Bank of New Zealand	-25 b.p.	3.00		
29	Bank of Brazil	+50 b.p.	14.25		
29	Federal Reserve	s.q.	0.25		
30	Bank of Mexico	s.q.	3.00		
<b>AUGUST</b>					
4	Reserve Bank of Australia	s.q.	2.00		
6	Bank of England	s.q.	0.50		
6-7	Bank of Japan	---	---		
12	Bank of Korea	s.q.	1.50		
<b>SEPTEMBER</b>					
1	Reserve Bank of Australia	s.q.	2.00		
2	Bank of Brazil	s.q.	14.25		
3	European Central Bank	s.q.	0.05		
3	Bank of Sweden	s.q.	-0.35		
9	Reserve Bank of New Zealand	-25 b.p.	2.75		
9	Bank of Canada	s.q.	0.50		
10	Bank of England	s.q.	0.50		
10	Bank of Korea	s.q.	1.50		
14-15	Bank of Japan	---	---		
17	Swiss National Bank	s.q.	-0.75		
17	Federal Reserve	s.q.	0.25		
21	Bank of Mexico	s.q.	3.00		
24	Bank of Norway	-25 b.p.	0.75		
<b>OCTOBER</b>					
5	Reserve Bank of Australia	s.q.	2.00		
6-7	Bank of Japan	---	---		
8	Bank of England	s.q.	0.50		
14	Bank of Korea	s.q.	1.50		
21	Bank of Brazil	s.q.	14.25		
21	Bank of Canada	s.q.	0.50		
22	European Central Bank	s.q.	0.05		
28	Reserve Bank of New Zealand	s.q.	2.75		
28	Bank of Sweden	s.q.	-0.35		
28	Federal Reserve	s.q.	0.25		
29	Bank of Mexico	s.q.	3.00		
30	Bank of Japan	---	---		
<b>NOVEMBER</b>					
2	Reserve Bank of Australia	s.q.	2.00		
5	Bank of England	s.q.	0.50		
5	Bank of Norway	s.q.	0.75		
11	Bank of Korea	s.q.	1.50		
18-19	Bank of Japan	---	---		
25	Bank of Brazil	s.q.	14.25		
30	Reserve Bank of Australia	s.q.	2.00		
<b>DECEMBER</b>					
2	Bank of Canada	s.q.	0.50		
3	European Central Bank	s.q.	0.05		
9	Bank of Korea	s.q.	1.50		
9	Reserve Bank of New Zealand	-25 b.p.	2.50		
10	Bank of England	s.q.	0.50		
10	Swiss National Bank	s.q.	-0.75		
15	Bank of Sweden	s.q.	-0.35		
16	Federal Reserve	+25 b.p.	0.50		
17	Bank of Norway	s.q.	0.75		
17	Bank of Mexico	s.q.	3.00		
17-18	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. \* To be determined.