



## FEDERAL RESERVE

### The Federal Reserve finally calls for a second rate hike!

#### ACCORDING TO THE FEDERAL RESERVE

- The Committee decided to raise the target range for the federal funds rate to 0.50% to 0.75%.
- 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 November indicates that the labor market has continued to strengthen and that economic activity has been expanding at a moderate pace since mid-year. Job gains have been solid in recent months and the unemployment rate has declined. Household spending has been rising moderately but business fixed investment has remained soft.
- Inflation has increased since earlier this year but is still below the Committee's 2% longer-run objective, partly reflecting earlier declines in energy prices and in prices of non-energy imports. Market-based measures of inflation compensation have moved up considerably but still are low; most survey-based measures of longer-term inflation expectations are little changed, on balance, in recent months.

#### COMMENTS

Twelve months after the first increase, the Federal Reserve's (Fed) leaders opted for a second key interest rate hike in this cycle. A year ago, expectations did not call for such a long time between the two decisions. Keep in mind that the U.S. economy has been disappointing over that time. In addition, concerns about the global economy's health at the start of the year, the Brexit referendum in the United Kingdom and the uncertainties throughout the electoral period prevented the Fed from taking a second shot at hiking the key rate within that timeframe. The vibrancy of financial markets since Donald Trump's election and the improvements in several economic indicators made the task easier for the monetary policy committee members. In fact, the futures market has been expecting this rate increase for the past few weeks, with a probability of 100%.

In the shorter term, the Fed is not much more optimistic than it was in September or November. Its reading of the

economic situation included in the statement addressed the moderate economic growth. Moreover, the Fed leaders' forecasts include few changes. The annual variation in real GDP in the fourth quarter of 2016 is upgraded from 1.9% to 2.0%, while the forecast for 2017 has also been revised upward—from 2.0% to 2.1%. The forecast for unemployment has been downgraded by 0.1%, to 4.5%, by the end of 2017.

Despite this cautious view of the economy, the Fed's leaders hinted that key rates would rise at a faster pace in 2017, with three increases of 25 basis points expected. In September, only two increases were in the cards. As was the case in September, three increases are also expected in 2018 and in 2019.

Since the Fed expects economic growth in 2017 to mirror that in 2016, these three expected rate hikes contrast with the single increases in 2015 and in 2016. The low unemployment rate is probably giving them the impetus to speed things up. While this is difficult to detect in its economic forecasts, we can also assume that the Fed is counting on the positive impact of the tax and budget policies to be put forth by the new Trump administration. However, the rate hikes being considered differ widely from what the other central banks should be doing, which could further drive up the value of the U.S. dollar.

**Implications:** The door was wide open for a rate hike at this meeting and the Fed finally took the plunge. This rate increase was entirely expected, but the fact that the Fed is now calling for three rate hikes in 2017 is somewhat of a surprise. We must keep in mind that the Fed has often slashed the scope of its planned monetary firming measures. Our scenarios continue to call for only two key rate increases in 2017.

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## Schedule 2016 of Central Bank meetings

	<u>Decision</u>	<u>Rate</u>		<u>Decision</u>	<u>Rate</u>		
<b>JANUARY</b>			<b>JULY</b>				
13	Bank of Korea	s.q.	1.50	5	Reserve Bank of Australia	s.q.	1.75
14	Bank of England	s.q.	0.50	6	Bank of Sweden	s.q.	-0.50
20	Bank of Brazil	s.q.	14.25	13	Bank of Korea	s.q.	1.25
20	Bank of Canada	s.q.	0.50	13	Bank of Canada	s.q.	0.50
21	European Central Bank	s.q.	0.05	14	Bank of England	s.q.	0.50
27	Federal Reserve	s.q.	0.50	20	Bank of Brazil	s.q.	14.25
28	Reserve Bank of New Zealand	s.q.	2.50	21	European Central Bank	s.q.	0.00
29	Bank of Japan	s.q.	-0.10	27	Federal Reserve	s.q.	0.50
				28	Bank of Japan	s.q.	-0.10
<b>FEBRUARY</b>			<b>AUGUST</b>				
1	Reserve Bank of Australia	s.q.	2.00	2	Reserve Bank of Australia	-25 b.p.	1.50
4	Bank of England	s.q.	0.50	4	Bank of England	-25 b.p.	0.25
4	Bank of Mexico	s.q.	3.25	10	Bank of Korea	s.q.	1.25
11	Bank of Sweden	-15 b.p.	-0.50	10	Reserve Bank of New Zealand	-25 b.p.	2.00
15	Bank of Korea	s.q.	1.50	11	Bank of Mexico	s.q.	4.25
17	Bank of Mexico	+50 b.p.	3.75	31	Bank of Brazil	s.q.	14.25
29	Reserve Bank of Australia	s.q.	2.00				
<b>MARCH</b>			<b>SEPTEMBER</b>				
2	Bank of Brazil	s.q.	14.25	6	Reserve Bank of Australia	s.q.	1.50
9	Bank of Korea	s.q.	1.50	7	Bank of Sweden	s.q.	-0.50
9	Reserve Bank of New Zealand	-25 b.p.	2.25	7	Bank of Canada	s.q.	0.50
9	Bank of Canada	s.q.	0.50	8	European Central Bank	s.q.	0.00
10	European Central Bank	-5 b.p.	0.00	8	Bank of Korea	s.q.	1.25
14	Bank of Japan	s.q.	-0.10	15	Bank of England	s.q.	0.25
16	Federal Reserve	s.q.	0.50	15	Swiss National Bank	s.q.	-0.75
17	Bank of England	s.q.	0.50	21	Reserve Bank of New Zealand	s.q.	2.00
17	Bank of Norway	-25 b.p.	0.50	21	Bank of Japan	s.q.	-0.10
17	Swiss National Bank	s.q.	-0.75	21	Federal Reserve	s.q.	0.50
18	Bank of Mexico	s.q.	3.75	22	Bank of Norway	s.q.	0.50
				29	Bank of Mexico	+50 b.p.	4.75
<b>APRIL</b>			<b>OCTOBER</b>				
5	Reserve Bank of Australia	s.q.	2.00	3	Reserve Bank of Australia	s.q.	1.50
13	Bank of Canada	s.q.	0.50	12	Bank of Korea	s.q.	1.25
14	Bank of England	s.q.	0.50	19	Bank of Brazil	-25 b.p.	14.00
18	Bank of Korea	s.q.	1.50	19	Bank of Canada	s.q.	0.50
21	European Central Bank	s.q.	0.00	20	European Central Bank	s.q.	0.00
21	Bank of Sweden	s.q.	-0.50	27	Bank of Norway	s.q.	0.50
27	Reserve Bank of New Zealand	s.q.	2.25	27	Bank of Sweden	s.q.	-0.50
27	Bank of Brazil	s.q.	14.25	31	Reserve Bank of Australia	s.q.	1.50
27	Bank of Japan	s.q.	-0.10	31	Bank of Japan	s.q.	-0.10
27	Federal Reserve	s.q.	0.50				
<b>MAY</b>			<b>NOVEMBER</b>				
3	Reserve Bank of Australia	-25 b.p.	1.75	2	Federal Reserve	s.q.	0.50
5	Bank of Mexico	s.q.	3.75	3	Bank of England	s.q.	0.25
12	Bank of England	s.q.	0.50	9	Reserve Bank of New Zealand	-25 b.p.	1.75
12	Bank of Korea	s.q.	1.50	10	Bank of Korea	s.q.	1.25
12	Bank of Norway	s.q.	0.50	17	Bank of Mexico	+50 b.p.	5.25
25	Bank of Canada	s.q.	0.50	30	Bank of Brazil	-25 b.p.	13.75
<b>JUNE</b>			<b>DECEMBER</b>				
2	European Central Bank	s.q.	0.00	5	Reserve Bank of Australia	s.q.	1.50
7	Reserve Bank of Australia	s.q.	1.75	7	Bank of Canada	s.q.	0.50
8	Bank of Korea	-25 b.p.	1.25	8	European Central Bank	s.q.	0.00
8	Reserve Bank of New Zealand	s.q.	2.25	14	Federal Reserve	+25 b.p.	0.75
8	Bank of Brazil	s.q.	14.25	14	Bank of Korea	s.q.	1.25
15	Bank of Japan	s.q.	-0.10	15	Bank of England	s.q.	0.25
15	Federal Reserve	s.q.	0.50	15	Bank of Norway	s.q.	0.50
16	Bank of England	s.q.	0.50	15	Bank of Mexico	s.q.	0.50
16	Swiss National Bank	s.q.	-0.75	15	Swiss National Bank	s.q.	0.50
23	Bank of Norway	s.q.	0.50	19	Bank of Japan	s.q.	0.50
30	Bank of Mexico	+50 b.p.	4.25	21	Bank of Sweden	s.q.	0.50

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.