

FOMC minutes

Confirmation of a very divided committee – a Fed hike will depend on incoming data

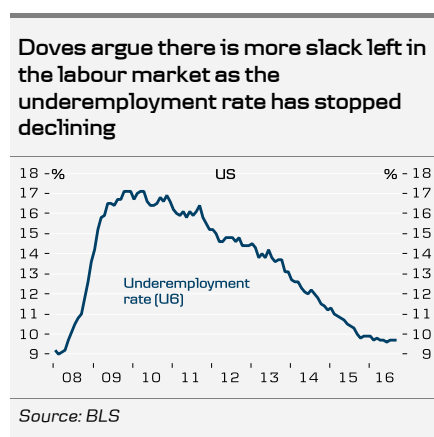
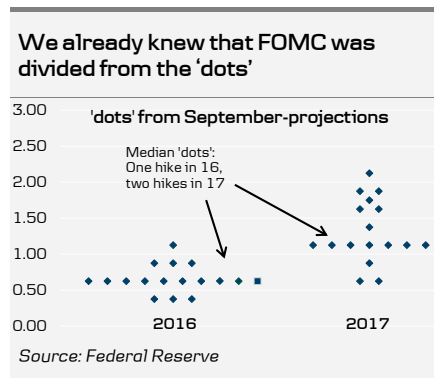
Bird fight

The FOMC minutes from the September meeting confirm that we are dealing with a very divided FOMC and that there is a ‘bird fight’ among the hawks and doves in the FOMC, see *FOMC review*. Hawks think that risks are that the economy overheats as employment has increased over the past six years and that low rates create financial instability. Doves think that there are signs that labour market slack has been larger than previously expected since the unemployment rate and underemployment rate have been flat for the past year. In their view, the Fed can afford to stay patient as core inflation runs below 2% and there is little sign of increasing underlying inflation pressure as wage growth is subdued.

We do not change our Fed call based on these minutes, as they confirm more or less what we already knew due to the many Fed speeches since the last meeting. **For now we stick to our non-consensus view that the Fed will stay on hold for the rest of the year, although it is a close call whether the Fed will hike or not in December.** The reason for our call is that the Fed seems too optimistic on Q3 GDP growth and we fear that economic data may continue to disappoint in the short term. **Incoming data will be important for the Fed’s decision to hike or not later this year.** The combination of weak GDP growth over the past three quarters, still slack left in the labour market, subdued wage growth, low inflation expectations and core inflation continuously running below the 2% target, means that the Fed can afford to stay patient. **A November hike seems unlikely due to the Presidential election just a week after the next FOMC meeting.**

As the jobs report was not the smoking gun for the Fed (see *Flash Comment*), we are looking forward to Friday, when we get retail sales data for September and Fed Chair Yellen is due to speak. Both could be important for our Fed call, as retail sales have been weak in July and August and since Yellen sounded more dovish at the press conference after the September meeting than the tone in the FOMC statement.

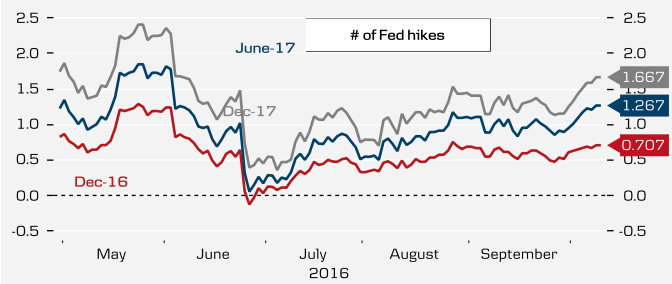
The market reaction to the minutes was muted. Markets have priced in a two-thirds probability of a hike by the turn of the year.



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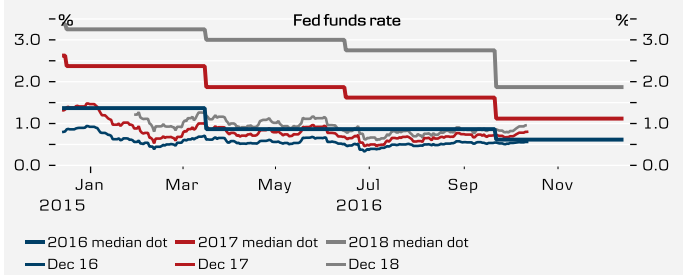
FOMC chart book

Markets have priced in a two-thirds probability of a hike by the turn of the year



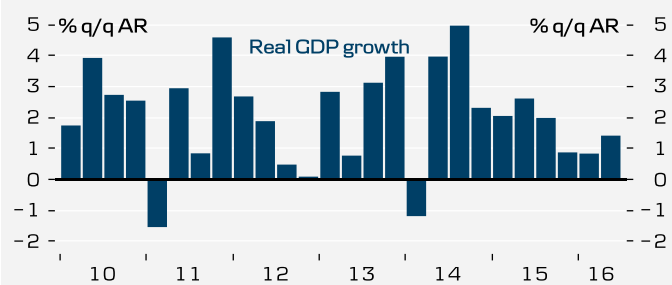
Source: Bloomberg

Markets still do not believe in 'dots'



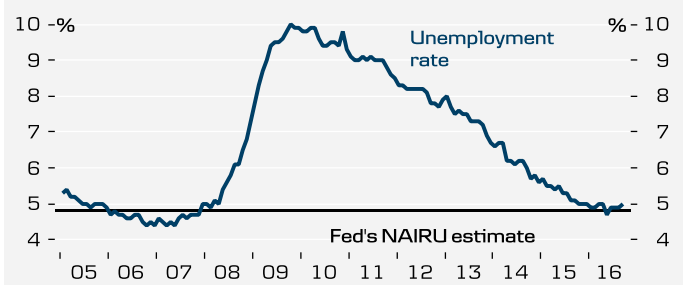
Source: Federal Reserve, Bloomberg

GDP growth has slowed markedly to just around 1% q/q AR for the past three quarters



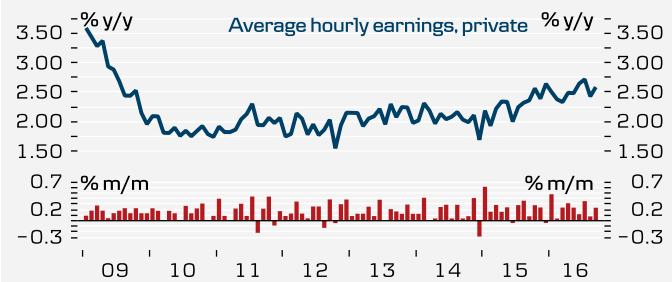
Source: BEA, Danske Bank Markets

Unemployment rate has moved sideways for some time



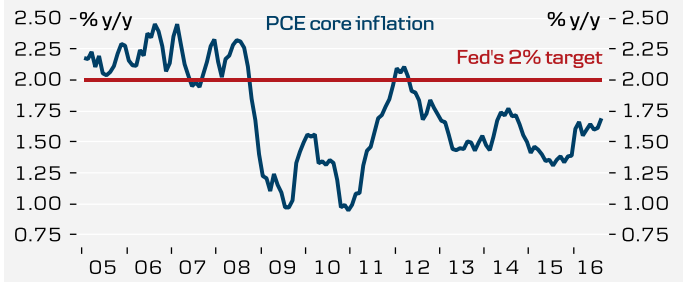
Source: BLS, Danske Bank Markets

Wage growth has picked up but is still subdued



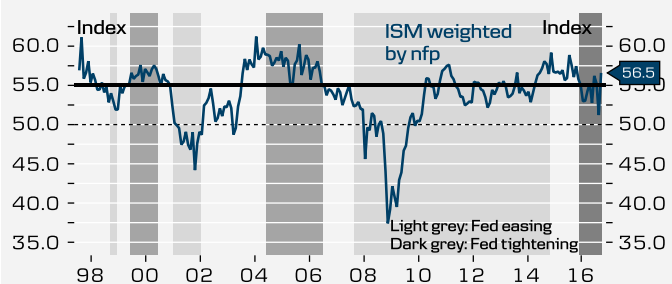
Source: BLS, Danske Bank Markets

PCE core inflation has moved sideways this year - it has only been at or above target for five months since 2008



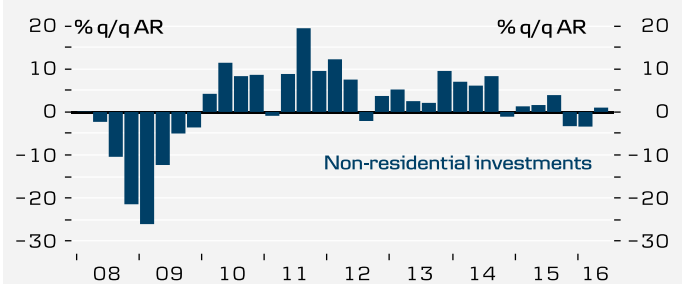
Source: BEA, Federal Reserve

Positive news that ISM has rebounded sharply



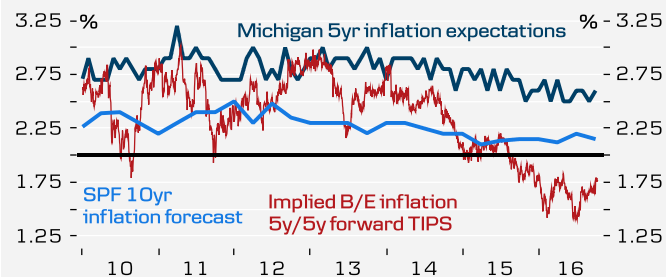
Source: ISM, BLS, Danske Bank Markets

Weak business investments



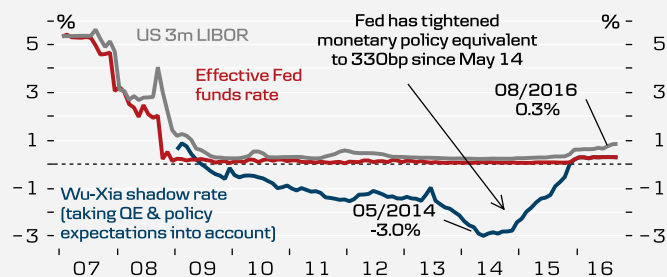
Source: BEA

Inflation expectations (both market-based and survey-based) have moved lower



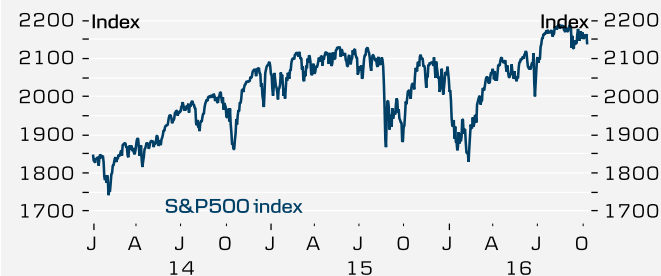
Source: Federal Reserve of Philadelphia, Macrobond Financial, University of Michigan, Danske Bank Markets

The Fed has already tightened monetary policy equivalent to 330bp due to QE tapering and hiking expectations



Source: Federal Reserve, Federal Reserve Bank of Atlanta, Macrobond

S&P500 has moved sideways for some time



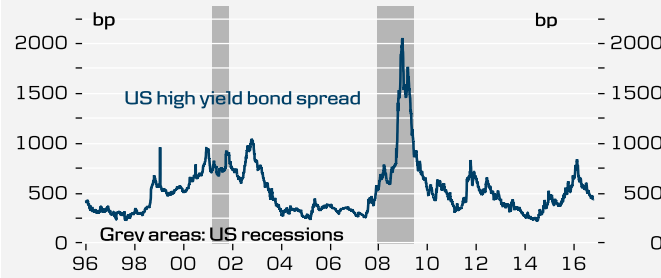
Source: Macrobond Financial

USD fairly stable lately but still relatively strong



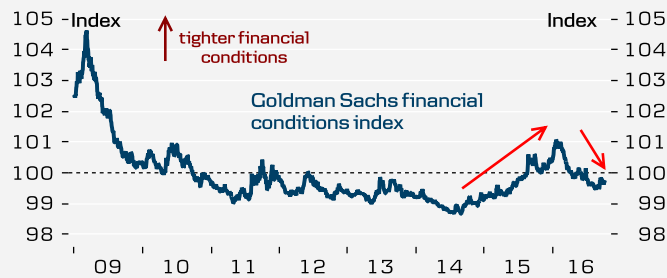
Source: Federal Reserve of Philadelphia, Macrobond Financial, University of Michigan, Danske Bank Markets

Credit spreads have declined but still large



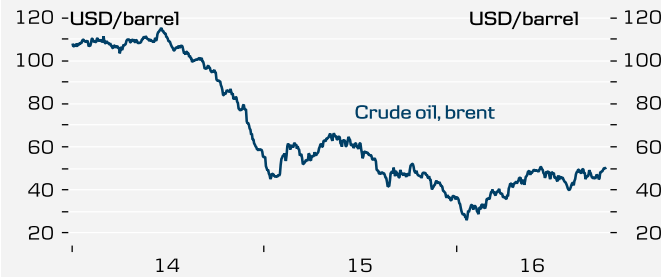
Source: Bloomberg

Financial conditions have eased



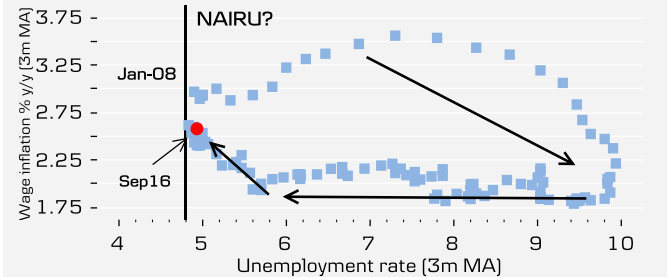
Source: Goldman Sachs, Federal Reserve, Danske Bank Markets

Oil prices have moved slightly up on OPEC stories



Source: EIA

Fed sees the world through the Phillips curve



Source: BLS, Danske Bank Markets

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None.

Date of first publication

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