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Economic Analysis

FOMC 2015: The Year of Liftoff

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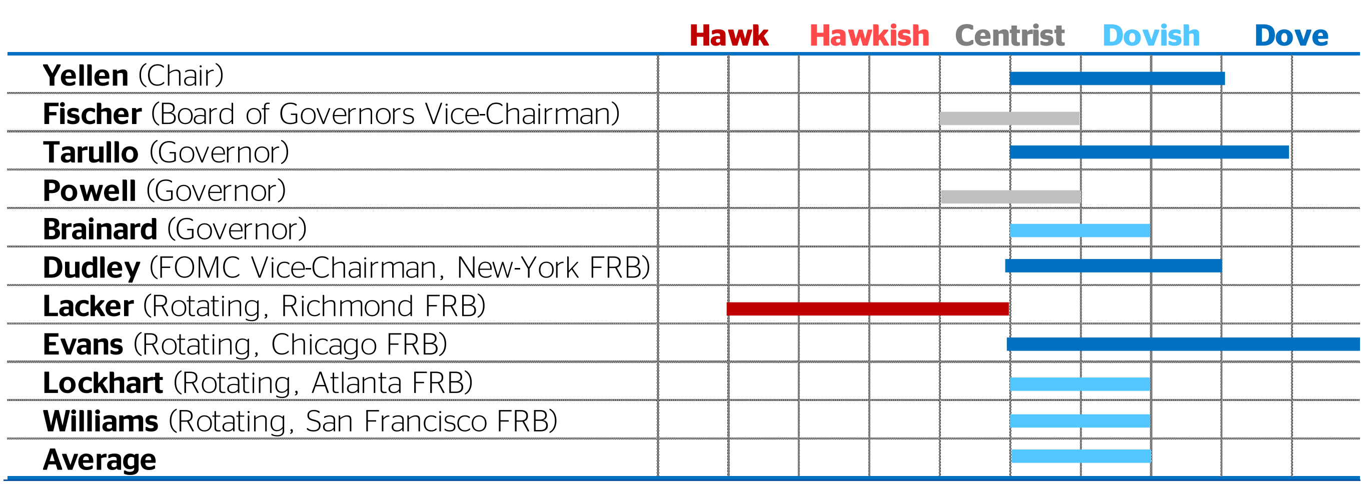
- **2015 FOMC on balance will remain centrist**
- **January meeting statement is expected to remain unchanged**
- **2015 Fed dilemma: taking on monetary normalization as dual mandate goals diverge**

The first year of Yellen's tenure as Fed Chair has proven to be a productive one with the end of QE3 and a firm hand on moving forward, yet with "patience," on monetary policy normalization. As expected, she carried on the traditions of ruling by consensus and maintaining commitment to transparency in Fed communication. The 2015 FOMC January meeting will bring on board new rotating members to vote: the four incoming 2015 voting members are Jeffrey Lacker (FRB Richmond), Charles Evans (FRB Chicago), Dennis Lockhart (FRB Atlanta), and John Williams (FRB San Francisco). Nevertheless, the voters' rotation will not change the centrist position of the FOMC and the Board of Governors that manifested itself in the 2H14. We expect Evans' dovish stance to be balanced with Lacker's hawkish views, while Lockhart and Williams will support the consensus and stay in the center, leaning lightly towards dovish "patient" attitude.

Jeffrey Lacker (FRB Richmond) has a reputation as a hawk and was the lone vote against the FOMC actions in 2012 (his last time voting). In 2012 he opposed the highly accommodative monetary policy stance and the asset purchase program. Yet this time around, his speeches indicate that he is comfortable with the consensus of a 2015 policy rate liftoff. All other things being equal: He is expected to support the FOMC majority position for at least the first several meetings.

> *"The FOMC has no pre-set timetable for raising the federal funds rate target. Policymakers should strive to look through transitory phenomena to assess the appropriate path for interest rates." Lacker, Jan 9, 2015*

Chart 1
Federal Funds Rate Futures (%)



Source: Bloomberg & BBVA Research

Charles Evans (FRB Chicago) is an established dove, who made his projections of the appropriate pace of tightening (FOMC dots) known by expressing his support of a policy rate liftoff in 1Q16 or later. Evans also voted against FOMC action twice in late 2011, soliciting for additional policy accommodation at that time.

> *"…my outlook for inflation over the next three years is for it to be less than 2 percent — even in 2017 it's just a touch below 2 percent in my outlook. And that's an outlook that's presuming a very high level of accommodative monetary policy that continues." Evans, December 3, 2014*

Both Dennis Lockhart (FRB Atlanta), and John Williams (FRB San Francisco) have previously taken dovish stances but in recent speeches are leaning toward the center. Both FRB presidents did not vote against a single FOMC action through the great recession and the conduct of the highly accommodative monetary.

> *"I feel the Fed is coming nearer to the end of our job as defined by those extraordinary circumstances, and anticipation of the normalization of monetary policy—interest rate policy—is appropriate. In that sense, I look for a new phase of policy to commence in 2015." Lockhar, January 12, 2015*

> *"It's still appropriate for us to start the process of normalizing monetary policy this year. The exact timing of that is going to depend on a data. If my forecasts come true, I think that sometime around the middle of a year we will be closer to the decision."Williams, January 16, 2015*

The January FOMC meeting is not expected to result in any alterations to the policy statement. Furthermore, similar to January 2014, we expect a unanimous vote for the policy action due to rotation of voting members. The FOMC is also expected to revisit its statement from January 2012 on the "Long Term Goals and Policy Strategy." While there will be pressure within the FOMC to revise the inflation target, with an explicit commitment to a symmetric inflation target, the likelihood of the FOMC to make any adjustments to the inflation wording is very low.

The Fed's 2015 challenge is the divergence in the dual mandate goals, as the FOMC will continue to face an economic environment of strong growth and employment but persistent downward pressure on inflation. Therefore, some of the Committee members' opinions on the timing and the pace of policy normalization will deviate from the majority stance as the decision day rolls closer. We maintain our baseline scenario for a liftoff in mid-2015.