

Economic Analysis

Weekly Focus: FOMC Minutes and CPI Inflation

Kim Fraser Chase

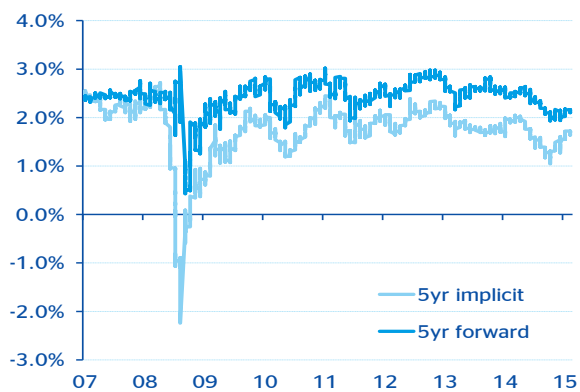
Low Inflation Still Holding Back the First Rate Hike Until at Least September

Two releases dominate the economic calendar this week: the **FOMC meeting minutes (Wednesday)** and **April's CPI report (Friday)**. The minutes are expected to clarify the changes to April's FOMC statement which acknowledged the slowdown in first quarter economic activity as well as developments in inflation trends ([see brief](#)). Given the statement's increased focus on inflation – not only energy prices but import prices as well – the minutes will likely set the stage for a market-moving CPI release to end the week.

The addition of import prices in the FOMC statement reflects the Committee's increased concerns over the USD appreciation and suggests that they may expect downward pressure on core inflation in the coming months. This opens the door for more uncertainty in the future as the Committee remains on edge, taking upcoming economic data day by day. Although we have seen some upward pressures from energy prices in April (crude oil prices up near \$60/bbl), import prices for the month declined much more than expected, down 0.3% to mark the tenth consecutive monthly decline. On a YoY basis, import prices have sharply decelerated to -10.7%, the slowest pace since mid-2009. This does not bode well for the upcoming CPI report, which we expect to just barely break into positive growth for the month.

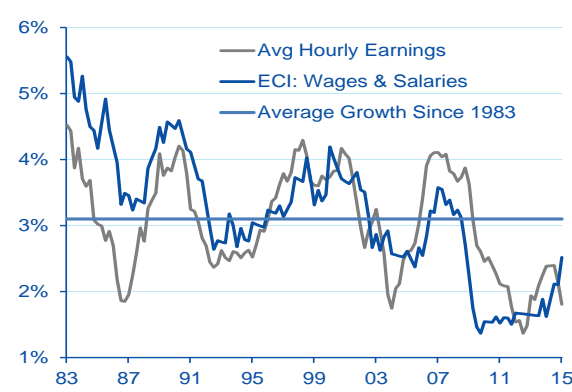
Surprisingly, inflation expectations are on the rise. The Atlanta Fed's Business Inflation Expectations Survey noted an increase in the expected change in unit costs over the next 12 months from 1.7% in April to 1.9% in May. This may be largely due to the gradual increase in oil prices throughout the past month as well as the latest indicators on stronger wage growth (particularly the Employment Cost Index). However, expectations are still well-below where they were this time last year, and the data do not point to an inflation rate at the Fed's target of 2.0% until at least 2016. We do not expect that inflation expectations will increase enough to convince the Fed to raise rates in June, but by September we are likely to be at more comfortable levels. Both the meeting minutes and the CPI data should confirm these projections for the first federal funds rate hike in September, with a gradual pace of rate increases thereafter.

Graph 1
Inflation Expectations (%)



Source: FRB & BBVA Research

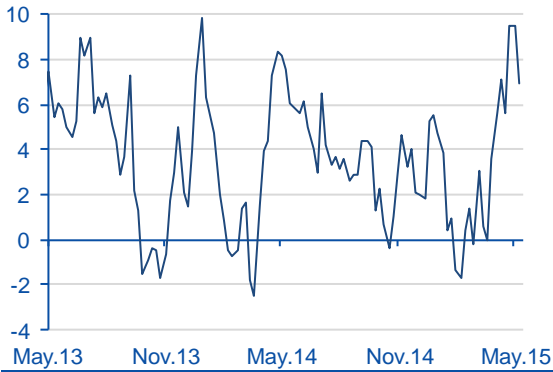
Graph 2
Wage Growth (%)



Source: BLS & BBVA Research

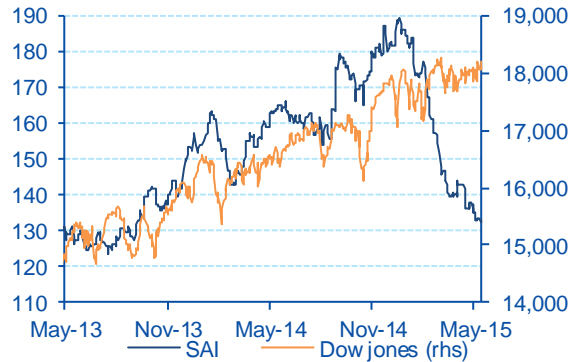
Economic Trends

Graph 3
BBVA USA Weekly Activity Index (3 month % change)



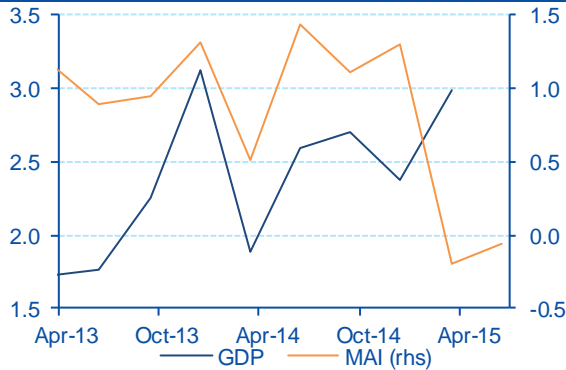
Source: BBVA Research

Graph 4
BBVA USA Surprise Activity Index & Dow Jones (Index 2009=100 & eop)



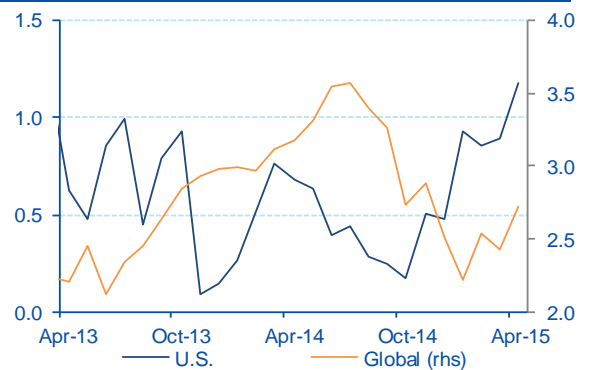
Source: Bloomberg & BBVA Research

Graph 5
BBVA USA Monthly Activity Index & Real GDP (4Q % change)



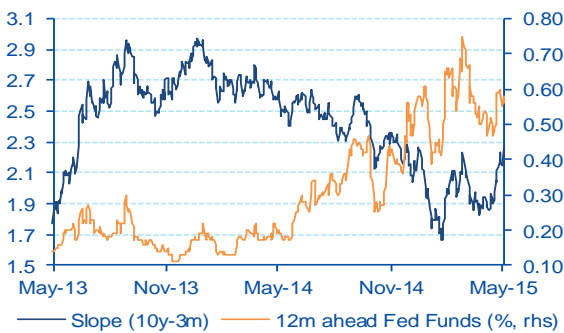
Source: BBVA Research & BEA

Graph 6
BBVA USA Risk Index (> 0 = increasing risk)



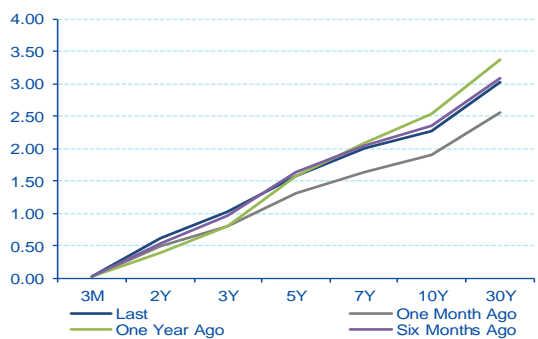
Source: BBVA Research

Graph 7
Fed Futures & Yield Curve Slope (% & 10year-3month)



Source: Haver Analytics & BBVA Research

Graph 8
U.S. Treasury Yield Curve (% p.a.)



Source: Haver Analytics & BBVA Research

Week Ahead Economic Calendar

Date	Event	Period	BBVA	Consensus	Previous
18-May	National Association of Home Builders Market Index SA	MAY	57.00	57.00	56.00
19-May	US New Privately Owned Housing Units Started by Structure Total SAAR	APR	955.00	1020.00	926.00
19-May	Private Housing Units Started by Structure Total Monthly % Change SA	APR	3.13	10.15	2.00
19-May	Private Housing Authorized by Bldg Permits by Type Total SAAR	APR	1080.00	1070.00	1042.00
19-May	Private Total Housing Authorized by Building Permits MoM SA	APR	3.65	2.69	-5.40
21-May	US Initial Jobless Claims SA		271.00	273.00	264.00
21-May	US Continuing Jobless Claims SA		2235.00	2231.50	2229.00
21-May	Chicago Fed National Activity Index	APR	-0.10	-	-0.42
21-May	Philadelphia Fed Business Outlook Survey Diffusion Index General Conditions	MAY	9.30	8.00	7.50
21-May	Conference Board US Leading Index MoM	APR	0.20	0.30	0.20
21-May	US Existing Homes Sales SAAR	APR	5.13	5.22	5.19
21-May	US Existing Homes Sales MoM SA	APR	-1.16	0.61	6.13
22-May	US CPI Urban Consumers MoM SA	APR	0.10	0.10	0.24
22-May	US CPI Urban Consumers Less Food & Energy MoM SA	APR	0.10	0.20	0.23

Economic Outlook

	2014		2015		2014	2015	2016	2017
	4Q	1Q	2Q	3Q				
Real GDP (% SAAR)	2.2	0.2	3.6	5.0	2.4	2.9	2.8	2.8
CPI (YoY %)	1.2	-0.1	0.2	0.7	1.6	0.6	1.9	2.2
CPI Core (YoY %)	1.7	1.7	1.6	1.7	1.7	1.6	1.7	1.9
Unemployment Rate (%)	5.7	5.6	5.4	5.2	6.2	5.3	4.9	4.6
Fed Target Rate (eop, %)	0.25	0.25	0.25	0.50	0.25	0.50	1.50	2.50
10Yr Treasury (eop, % Yield)	2.21	2.04	1.90	2.32	2.21	2.40	3.00	3.54
US Dollar/ Euro (eop)	1.23	1.08	1.00	1.00	1.23	1.02	1.12	1.24
Core Logic Home Prices (YoY %)	4.99	5.23	5.64	5.30	7.45	5.29	4.85	4.38

Fun Fact

71% of Millennials (those born between 1981 and 2000) would rather go to the dentist than listen to what banks are saying. (Millennial Disruption Index, Viacom)

Recent Publications

[U.S. Economic Outlook 2Q15](#) (May 13, 2015)

[Employment Situation Back on Track in April](#) (May 8, 2015)

[FOMC Review of Economic Activity Hints at Rate Hike After June](#) (April 29, 2015)

[Weak 1Q GDP Continues for 7th Straight Year](#) (April 29, 2015)

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