

Economic Analysis

# Weekly Focus: FOMC Minutes and Inflation

Kim Chase

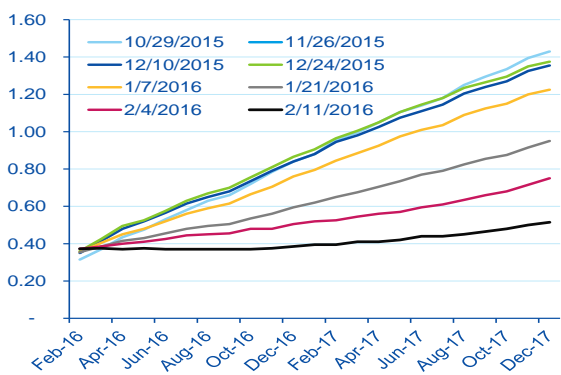
## January's FOMC Minutes Will Further the Case for Delaying the Next Rate Hike

**The FOMC minutes (Wednesday)** will be the topic to watch for this week. However, so much has happened in the global economy since the January meeting that the details may not be as relevant to the Fed's current discussion. We expect that the minutes will highlight some members' growing concerns on global economic and financial market uncertainties, as well as continued worries on persistently low inflation. There may not be any direct mention of plans to revise down their policy path projections, but current conditions suggest that this idea must at least be running through their minds. The January meeting opened the door for the FOMC to hold off on increasing rates in March, and Yellen's testimony to Congress furthered such concerns. Questions on the possibility of negative interest rates have sent markets into a frenzy, despite the fact that Yellen made it clear that she does not foresee that such a drastic policy move will be necessary. Federal funds rate futures suggest that markets are now expecting the Fed to hold off on another rate hike for the entire year, which seems a bit too hasty of an assumption at the moment. Still, the FOMC's data-dependent strategy lends itself to such a scenario if economic and financial conditions continue to deteriorate. At this point, it seems too early to know for sure. Hopefully the meeting minutes will provide some clarity on what direction the FOMC is headed.

## No Signs of a Reversal in Headline CPI or Inflation Expectations Anytime Soon

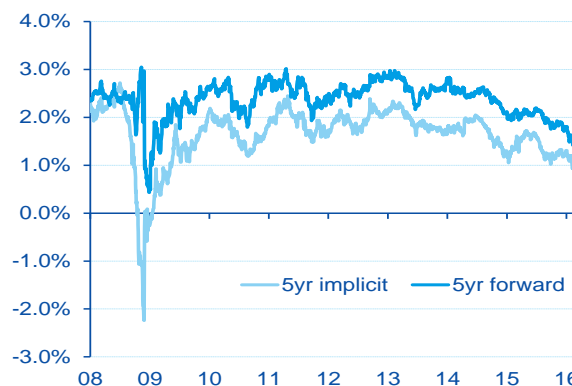
**January's CPI report (Friday)** goes hand in hand with the FOMC minutes, with current conditions pointing to increased downward pressure on inflation compared to last month. Oil prices have dropped below \$30/barrel and inflation expectations have continued to fall, reaching seven-year lows. Chair Yellen, in her testimony to Congress, acknowledged the latest trends in low prices and market-based measures on inflation compensation but also remains adamant that downward pressures will soon fade once oil prices start to rise again. The problem is that signs are not pointing to a rise in prices anytime soon, so it will be interesting to see how long the FOMC hangs onto this sentiment before admitting to more serious concerns on low inflation. In the meantime, we expect to see continued declines in headline CPI and only modest gains in the core figure.

Graph 1  
**Federal Funds Rate Futures (%)**



Source: Bloomberg & BBVA Research

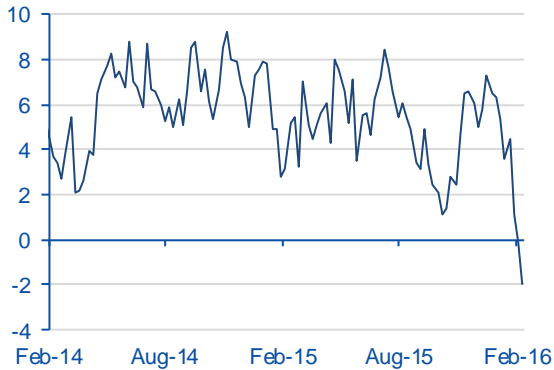
Graph 2  
**Inflation Expectations (%)**



Source: FRB & BBVA Research

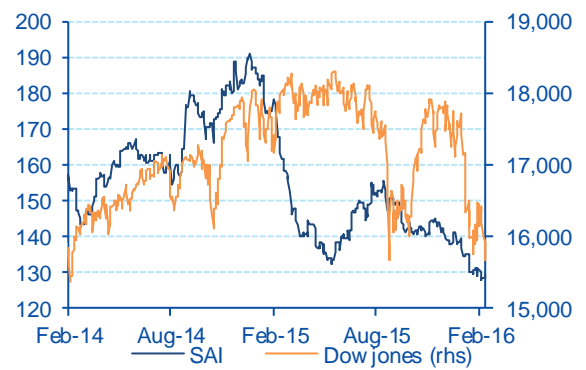
**Economic Trends**

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



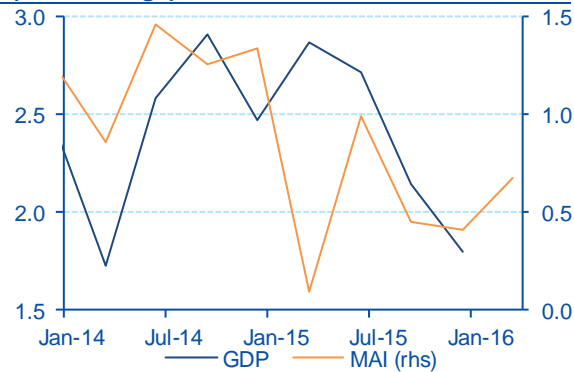
Source: BBVA Research

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



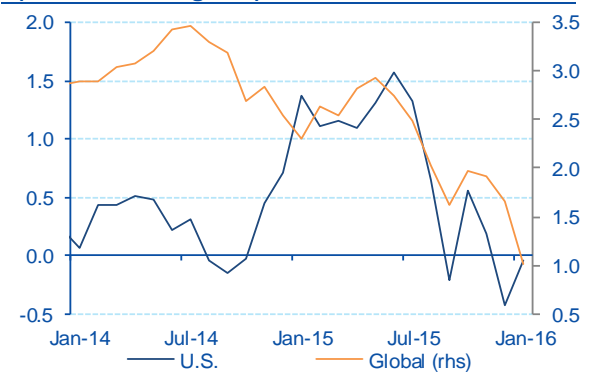
Source: Bloomberg & BBVA Research

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



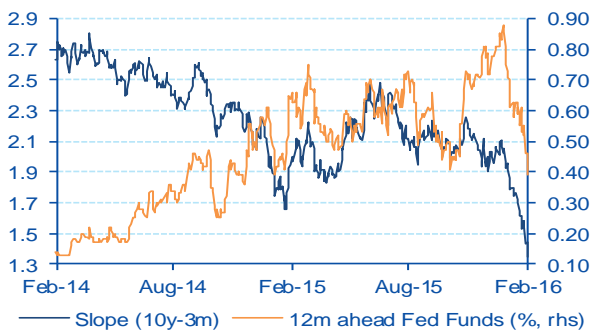
Source: BBVA Research & BEA

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



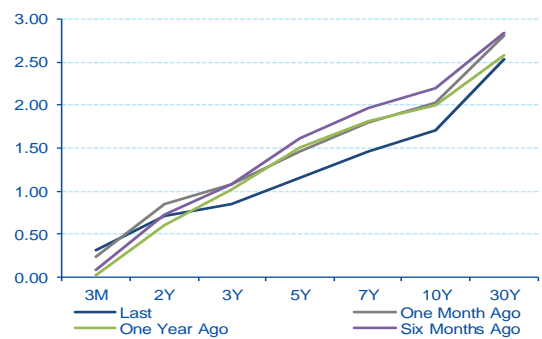
Source: BBVA Research

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
16-Feb	US Empire State Manufacturing Survey General Business Conditions SA	FEB	-9.70	-10.50	-19.37
16-Feb	National Association of Home Builders Market Index SA	FEB	59.00	60.00	60.00
17-Feb	US New Privately Owned Housing Units Started by Structure Total SAAR	JAN	1198.00	1175.00	1149.00
17-Feb	Private Housing Units Started by Structure Total Monthly % Change SA	JAN	4.26	2.26	-2.50
17-Feb	Private Housing Authorized by Bldg Permits by Type Total SAAR	JAN	1231.00	1200.00	1204.00
17-Feb	Private Total Housing Authorized by Building Permits MoM SA	JAN	2.24	-0.33	-6.10
17-Feb	US PPI Final Demand MoM SA	JAN	-0.20	-0.20	-0.20
17-Feb	US PPI Final Demand Less Foods and Energy MoM SA	JAN	0.00	0.10	0.20
17-Feb	US Industrial Production MOM SA	JAN	-0.20	0.35	-0.36
17-Feb	US Capacity Utilization % of Total Capacity SA	JAN	76.30	76.70	76.49
17-Feb	US Industrial Production Industry Groups Manufacturing MoM SA	JAN	-0.10	0.25	-0.10
18-Feb	US Initial Jobless Claims SA	FEB 13	273.00	275.00	269.00
18-Feb	US Continuing Jobless Claims SA	FEB 6	2235.00	2250.00	2239.00
18-Feb	Philadelphia Fed Business Outlook Survey Diffusion Index General Conditions	FEB	-2.90	-3.00	-3.50
18-Feb	Conference Board US Leading Index MoM	JAN	-0.10	-0.20	-0.20
19-Feb	US CPI Urban Consumers MoM SA	JAN	-0.20	-0.10	-0.10
19-Feb	US CPI Urban Consumers Less Food & Energy MoM SA	JAN	0.00	0.20	0.10

## Economic Outlook

	2015		2016		2014	2015	2016	2017
	3Q	4Q	1Q	2Q				
Real GDP (% SAAR)	2.0	0.7	1.5	3.0	2.4	2.4	2.5	2.4
CPI (YoY %)	0.1	0.5	1.1	1.1	1.6	0.1	1.7	1.9
CPI Core (YoY %)	1.8	2.0	2.1	2.1	1.7	1.8	2.0	2.0
Unemployment Rate (%)	5.2	5.0	5.0	4.9	6.2	5.3	4.9	4.6
Fed Target Rate (eop, %)	0.25	0.50	0.50	0.75	0.25	0.50	1.00	2.00
10Yr Treasury (eop, % Yield)	2.17	2.24	2.15	2.17	2.21	2.24	2.43	3.09
US Dollar/ Euro (eop)	1.12	1.09	1.05	1.06	1.23	1.09	1.12	1.16
Core Logic Home Prices (YoY %)	4.86	5.51	5.86	5.86	7.69	4.99	5.37	2.45

## Fun Fact

Since World War II, the first or second place winner in New Hampshire has gone on to win the GOP nomination. (NBC, February 2016)

## Recent Publications

- [Oil Prices: Black Gold or a Black Hole?](#) (February 12, 2016)
- [January Retail Sales Provide Strong Start to 1Q16](#) (February 12, 2016)
- [Yellen's Testimony Highlights Growing Concerns](#) (February 10, 2016)
- [U.S. Recession Probability Rises to 25%](#) (February 5, 2016)
- [Payrolls Soft but UR at Record Low in January](#) (February 5, 2016)
- [Senior Loan Officer Survey, January 2016](#) (February 2, 2016)
- [4Q15's 0.7% Pace Closes out 2015 at 2.4%](#) (January 29, 2016)
- [FOMC Statement: January 26-27<sup>th</sup> Meeting](#) (January 27, 2016)

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