

April FOMC meeting: Prospect of higher fed funds rates by year-end still on the cards

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As expected, the Federal Reserve left its monetary policy stance unchanged at the 28-29 April meeting. According to the post-meeting statement,¹ the economic slowdown in the first quarter of the year reflected in part temporary factors. Although the recovery in the labor and housing markets slowed somewhat and exports and business fixed investment declined significantly during the early months of this year, the Committee probably expects private consumption to rebound in the coming months as “households’ real incomes rose strongly, partly reflecting earlier declines in energy prices, and consumer sentiment remains high”. This argument is in line with the March improvement in auto and retail sales, suggesting an improved outlook for private consumption.

The forward-looking parts of the FOMC policy statement were basically unchanged. Notwithstanding Q1 GDP soft patch, the Committee still expects activity to expand at a moderate pace in the quarters ahead, labor market indicators to continue moving toward levels consistent with its dual mandate and inflation to return to its medium-term target of 2.0%.

In our view, the March FOMC statement supports expectations for higher interest rates later this year. Given the recent economic slowdown in Q1, we stick to our view that the Central Bank will start its monetary normalization process in September, at the earliest. Nevertheless, we do not rule out entirely the possibility of the Fed delaying the first interest rate increase until Q4 2015, especially if inflation remains well below its medium-term 2% inflation target.

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¹ <http://www.federalreserve.gov/newsevents/press/monetary/20150429a.htm>

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