

Stage set for a FOMC rate hike in March

FOMC members that were scheduled to speak this week have sent a unified message. As Governor Lael Brainard put it *"the US economy is closing in on full employment, inflation is moving gradually toward the FOMC target, foreign growth is on more solid footing, and risks to the outlook are as close to balanced as they have been in some time"*. A point of view that appears to be shared by Chair Yellen who added that *"at our meeting later this month, the Committee will evaluate whether employment and inflation are continuing to evolve in line with our expectations, in which case a further adjustment of the federal funds rate would likely be appropriate"*.

It took a week for FOMC members to drive up market expectations for a hike in March



Chair Yellen could not have been more transparent about the FOMC intention to rise the fed funds target rate at the March meeting. It would take an awful job report on March 10 to stop the FOMC. Indeed, Chair Yellen estimates the longer-run trend in labour force growth is between 75K and 125K, so anything in that range or above would give the FOMC the green light to hike rates on March 15th.

With the annual core PCE inflation rate running at 1.7% and the New York Fed estimating that the current real neutral rate in 2017 is 0.5%, this calls for a faster pace of monetary policy normalization going forward than what was delivered in the previous 2 years. In that context, 3 rate hikes of 25 bps in 2017 appear the most likely scenario, unless unanticipated developments adversely affect the economic outlook.

Bottom-line: FOMC members have shown less patience for more clarity on the fiscal side than we thought and stand ready to make a move in March. Our base case scenario now includes 3 rate hikes in 2017 instead of only two. We have not altered our year end forecast for 10-year Treasury yields.

P. A. Ponsouxault

Rate forecast

United States

Quarters	Fed Fund	2YR	10YR
03/03/17	0.75	1.31	2.49
Q1/17	1.00	1.38	2.61
Q2	1.00	1.55	2.73
Q3	1.25	1.72	2.82
Q4	1.50	1.86	3.01
Q1/18	1.75	1.99	3.10
Q2	1.75	2.10	3.18
Q3	2.00	2.51	3.23
Q4	2.25	2.54	3.29

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