THE NATION
www.nationmultimedia.com

US rate hike expected as Fed meeting looms

December 15, 2015 10:03 am

WASHINGTON - The US Federal Reserve is widely expected to finally push interest rates up after seven years at the zero level when it opens a two-day policy meeting on Tuesday.

The break, well-flagged by Fed officials including Chair Janet Yellen, would signify leaving behind the extraordinary crisis stance in monetary policy that aimed to restore the US economy's strength after the financial crisis and deep recession of 2008-2009.

While an increase in the federal funds rate -- which has not been moved higher in almost a decade -- is not certain, Yellen strongly pointed to it at the beginning of December.

Since then, economic data, including job creation and consumer spending, have been strong enough to keep her from changing her view.

The Fed's policy body, the Federal Open Market Committee, will weigh over Tuesday and Wednesday whether the US economy is sufficiently strong to weather increasing the fed funds rate from 0-0.25 percent to an expected 0.25-0.50 percent.

The benchmark rate is a short-term peg for interbank lending which influences rates throughout the financial system.

Most importantly, expectations about its future level determine long-term interest rates on car and home loans, financing for businesses and foreign governments, and savers' deposits.

The prospect of the launch of a campaign to raise the rate and tighten US monetary policy after years of cheap dollars has already stirred turmoil in the global financial system, hurting especially emerging-market economies with significant dollar exposure and weakening currencies.

It will come as leading central banks elsewhere, including China, Japan and the eurozone, are easing monetary policy to boost growth.

- 'Calibrating' policy -

But even with a 0.25 percentage point increase, US rates would still be extraordinarily low, far below what the Fed considers a "normal" monetary stance.

Yellen has stressed that the Fed still wants to see more tightening in the labor market and to push inflation up, and that means continued low rates to support stronger growth.

"The Fed is not trying to slow down a fast-growing economy or dampen runaway inflation," Sam Stovall, equity strategist at S&P Capital IQ. A hike would be "an attempt to recalibrate, not restrain."

Extremely weak inflation, though, is a key reason why many in the FOMC have resisted, arguing that there is time to wait before liftoff.

However, Yellen argued in a December 2 speech that if the Fed waits too long,"we would likely end up having to tighten policy relatively abruptly to keep the economy from significantly overshooting both of our goals."

With the first rate hike already presumed, the greater question is, what happens next?

Yellen has repeatedly said that the liftoff from zero will initiate a series of increases whose pace will depend on how the economy reacts -- slower if there is weakness, and faster if it picks up strength.

For that reason, most eyes will be on what the Fed and Yellen say in statements and in forecasts about their expectations for economic growth and the expected level of the fed funds rate at the end of 2016 and 2017.

"There is a large gap between financial markets' expectation of the path of rates and the FOMC's expectation," said Deutsche Bank in a client note.

Deutsche Bank noted that markets on average are expecting just two increases next year while in the FOMC's September projections four increases to end at about 1.5 percent were indicated.

If the Fed reiterates that stance, it could strengthen the dollar but also weigh down equity markets.

The impact of sinking oil prices aside, however, markets were relatively subdued Monday going into the meeting.

"Overall, markets are on edge," said David Levy of Kenjol Capital Management. "There is not a lot a reason to get ahead of the Fed and step and be a buyer today.

AFP
http://www.nationmultimedia.com/breakingnews/US-rate-hike-expected-as-Fed-meeting-looms-30274953.html