



Fedwatch

April 8, 2008

FOMC Minutes March 18th Meeting

- Fed more worried on downside risks to growth
- Strains in financial markets continued to pose significant uncertainty to the economic outlook
- We expect further monetary policy easing

FOMC more pessimistic on economic activity

FOMC minutes continued to reflect a more pessimistic view on economic activity and increased downside risks to growth.

According to the Fed:

- The contraction in homebuilding intensified
- Consumer spending appeared to be weakening
- Industrial production fell in February
- Labor demand softened markedly in all sectors (except non businesses sector and state and local governments)
- Unemployment edged down to 4.8 in February but labor force participation rate declined.
- On the bright side, exports have risen sharply since December. Imports also increased but this was mainly due to oil imports. Most other categories of imports dropped in December and January on net, especially automotive and consumer goods.

In the forecast prepared for this meeting, the staff revised down its real GDP growth projection in 2008: expecting a contraction in 1S08 followed by a slow rise in 2S08. They expect GDP growth above potential in 2009.

On inflation, the Fed was disappointed by the increase of CPI. But most participants expected inflation to moderate later this year as growth in the US and abroad weakens, which would contribute to a flattening of oil and other commodities prices over time. As expected, the two dissenting votes to March action highlighted these inflationary pressures and advised to be patient until the full effect of previous policies take effect.

Board members noted that price discovery for mortgage-related financial assets had become increasingly difficult, raising the uncertainty around the balance sheet of financial institutions and intensifying the stress in financial markets. They agree that new liquidity facilities are being helpful.

FOMC will cut rates again in next meeting

Minutes reflect that FOMC members were significantly worried on GDP growth and the health of the financial sector. They were also increasingly worried about inflation, but less so at present. We expect FOMC to discuss a 25 or 50 bp cut on April 29th depending on incoming data.

Fed Funds: 2.25%
Next FOMC Meeting: April 29, 30

FOMC Meeting Minutes

March 18th, 2008

“Participants noted that the contraction in the housing sector had deepened and that considerable uncertainty surrounded the outlook for housing. Although some stabilization in housing markets was likely needed to help underpin an economic recovery in coming quarters, there was little indication that that process had yet begun. Elevated rates of foreclosures and large inventories of unsold property were likely to depress home prices for some time. Lower home prices would eventually buoy home buying, but in the meantime the prospect of continued price declines could lead potential homebuyers to defer purchases for a time, further damping housing activity and adding to downward pressure on home values. Participants noted that the trajectory of house prices was a major source of uncertainty in their economic outlook.”

“The forecast for core PCE price inflation over the first half of 2008 was raised in response to elevated readings in recent months. In addition, the forecast for headline PCE price inflation incorporated a much higher rate of increase for energy prices for the first half of the year; as a result, headline PCE price inflation was expected to substantially exceed core PCE price inflation in 2008. By 2009, the forecasts for both the headline and core PCE price indexes showed inflation receding from its 2008 level, in line with the previous forecasts.”

“... meeting participants regarded financial markets as unusually fragile. The new liquidity facilities recently introduced by the Federal Reserve would probably be helpful in bolstering market liquidity and promoting orderly market functioning, but even so, the ongoing strains were likely to raise the price and reduce the availability of credit to businesses and households. Evidence that an adverse feedback loop was under way, in which a restriction in credit availability prompts a deterioration in the economic outlook that, in turn, spurs additional tightening in credit conditions, was discussed. Several participants noted that the problems of declining asset values, credit losses, and strained financial market conditions could be quite persistent, restraining credit availability and thus economic activity.”