Economic Alert iQ

First Citizen
Research & Anal

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International
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Fed Decision Looms

- All eyes are on the U.S. Federal Reserve, which is widely expected to raise interest rates at the end of its meeting today.
- The U.S. is still adding jobs at a healthy pace, unemployment is low and wage growth continues to gain momentum.
- Those positive trends clear the way for the Fed to raise rates further. In addition to stronger than expected job reports for February, many market participants now expect another two increases in 2017, following the rate hike expected at today's meeting.
- Investment houses such as Goldman Sachs now see the Fed hiking not just in March but also in June. Morgan Stanley offers a similarly hawkish outlook, expecting two additional hikes in 2017 and have placed those in June and December, followed by four hikes in 2018.
- The announcement will come today at 2:00pm followed by a press conference by Chair Yellen at 2:30pm.

2017 FOMC Meetings	
May	2nd-3rd
June	13th-14th*
July	25th-26th
September	19th-20th*
Oct/Nov	31st-1st
December	12th-13th*

* Meeting associated with a Summary of Economic Projections and a press conference by the Chair.

According to Bloomberg the probability of a rate hike is 100%. At today's fed meeting, there is a 96% probability of a hike to 0.75-1.00 and a 4% probability of a hike to 1-1.25.

Current implied probabilities of a fed rate hike

Meeting	Prob Of Hike	Prob of Cut	0.75-1	1-1.25	1.25-1.5	1.5-1.75	1.75-2	2-2.25	2.25-2.5
03/15/2017	100.0%	0.0%	96.0%	4.0%	0.0%	0.0%	0.0%	0.0%	0.0%
05/03/2017	100.0%	0.0%	87.5%	12.1%	0.4%	0.0%	0.0%	0.0%	0.0%
06/14/2017	100.0%	0.0%	43.0%	50.5%	6.4%	0.2%	0.0%	0.0%	0.0%
07/26/2017	100.0%	0.0%	36.0%	49.3%	13.5%	1.2%	0.0%	0.0%	0.0%
09/20/2017	100.0%	0.0%	18.7%	42.9%	30.7%	7.1%	0.6%	0.0%	0.0%
11/01/2017	100.0%	0.0%	16.8%	40.4%	31.9%	9.5%	1.3%	0.1%	0.0%
12/13/2017	100.0%	0.0%	8.8%	29.1%	36.0%	20.2%	5.2%	0.6%	0.0%
01/31/2018	100.0%	0.0%	7.9%	27.1%	35.3%	21.8%	6.7%	1.1%	0.1%

Source: Bloomberg

U.S. Labor Market and Financial Sector Indicators

	Q1 16	***Q2 16***	***Q3 16***					***Q4 16***		
Indicator	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**
Unemployment Rate (%)	5.00	5.00	4.70	4.90	4.90	4.90	4.90	4.80	4.60	4.70
Initial Jobless Claims (weekly)	276	274	268	270	267	263	246	266	268	237
Continuing Claims (weekly)	2,189	2,165	2,112	2,117	2,160	2,142	2,050	2,043	2,007	2,093
Average Weekly Hours All Private Employees	34.40	34.40	34.40	34.40	34.40	34.30	34.40	34.40	34.30	34.40
Average Weekly Hours Non-Farm Private Employees	33.60	33.60	33.60	33.60	33.70	33.60	33.60	33.60	33.60	33.60
Total Employment in Labor Force (mn, sa)	151.30	151.00	151.10	151.10	151.50	151.70	151.90	151.90	152.00	152.1
Net Change in Total Employment in Labor Force (000s, sa)	258.00	-273.00	30.00	32.00	456.00	109.00	271.00	-24.00	146.00	63.00
Employment/Population Ratio (%)	59.90	59.70	59.70	59.60	59.80	59.70	59.80	59.70	59.70	59.70
Avg. Hourly Earnings (yoy %)	2.40	2.60	2.30	2.50	2.60	2.50	2.70	2.50	2.50	2.50
Avg. Hourly Earnings (mom %)	0.30	0.30	0.10	0.20	0.30	0.10	0.30	0.20	0.10	0.30
Fed Funds Rate (%)	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75
3-Month T-Bill Rate (%)	0.20	0.21	0.28	0.26	0.25	0.33	0.27	0.30	0.48	0.50
10-Year Treasury Yield (%)	1.77	1.83	1.85	1.47	1.45	1.58	1.59	1.83	2.38	2.44
Equity Market (S&P 500 Index)	2,060.00	2,065.00	2,097.00	2,099.00	2,174.00	2,171.00	2,168.00	2,126.00	2,199.00	2,239

Source: Bloomberg

Effects of Fed rate hike

- The Fed's actions have the potential to stir world markets. With the US being the world's biggest economy and the dollar being the world's reserve currency, any action by the country's central bank to influence the money supply has repercussions on the global financial markets.
- The US has been a major source of capital for emerging markets. The link has strengthened all the more since 2008-09 when the Fed launched its monetary stimulus known as quantitative easing (QE) and cut rates to near-zero.
- The monetary stimulus has been withdrawn and now the Fed is in the process of normalizing interest rates from the historic low rates. This has sparked worries that a portion of the US dollars invested because of the accommodative monetary policy will now flow back to the US since higher interest rates would strengthen

the US dollar relative to other currencies. This is exacerbated by the fact that many emerging market currencies have already slumped against the US dollar due to weakening macroeconomic fundamentals.

- Therefore, there may be increased capital outflows from many emerging markets if interest rate differentials are not adjusted, which may be difficult given the inflexibility they face when it comes to adjusting interest rates amid low and challenging economic growth.
- The U.S. equity market can take some hits when the Fed increases the fed fund rate because it costs companies more to borrow from financial institutions. Individuals are affected by increases to credit card and mortgage interest rates, especially if these loans carry variable interest rates. This has the effect of reducing the amount consumers can spend and invest.
- Less business spending can slow down the growth of a company; it might curtail expansions, mergers and even induce cutbacks. This can lead to a fall in earnings and for a public company, usually the stock price takes a hit.
- However, some sectors do benefit from interest rates hikes. One sector that tends to benefit is the financial sector. Banks, mortgage companies and insurance companies' earnings often increase because they can charge more for lending.

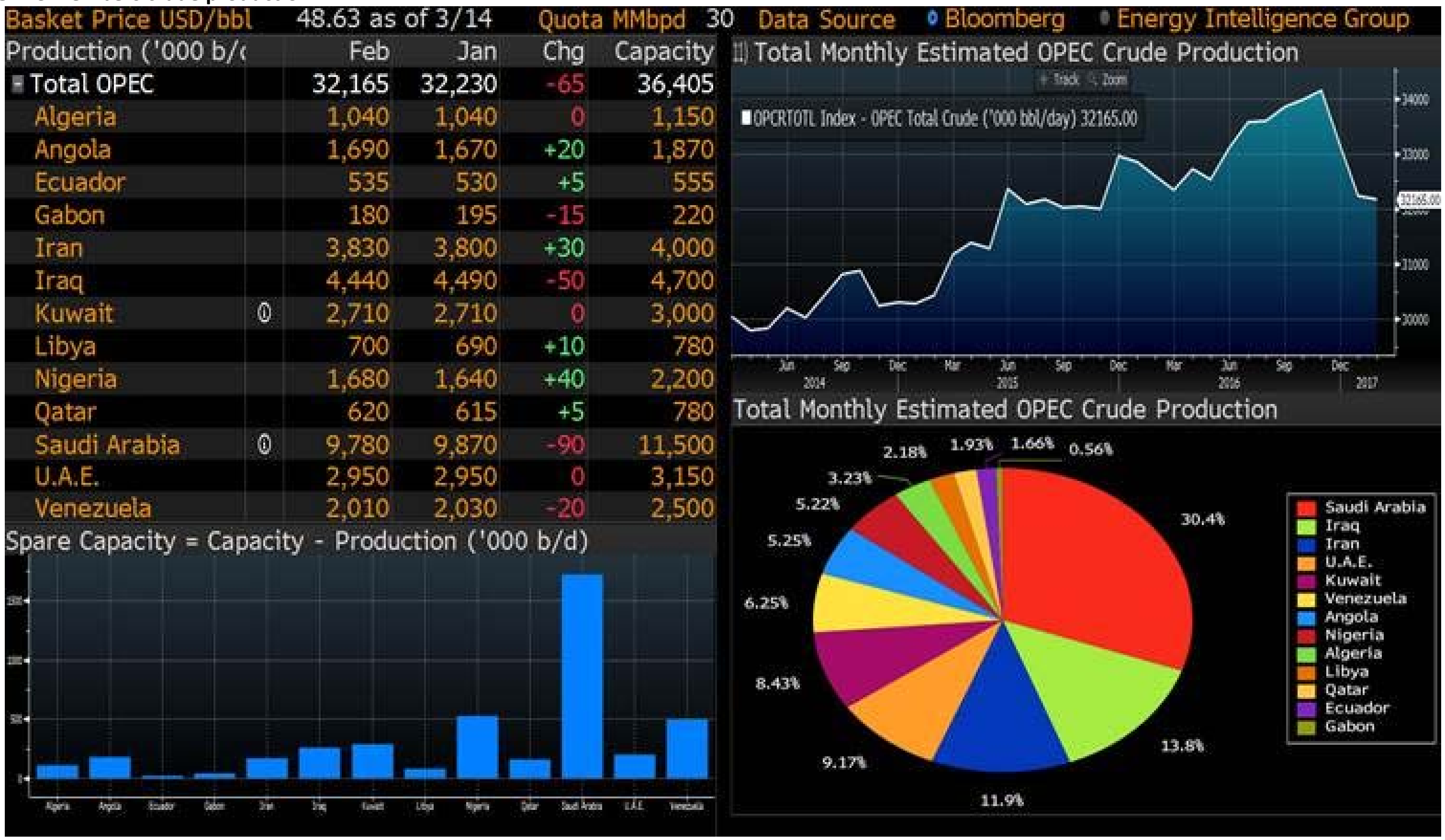
Rate hike impact on oil prices

- The oil markets will be keeping a close eye on developments, as any rate hike could push prices even lower from current levels.
- If crude oil market physical fundamentals hold steady with supply well ahead of demand, prices would take a hit from any strength in the dollar that resulted from an increase in interest rates.
- However, the impact can be mild and short term given that the Fed has telegraphed the rate hike for some time. In fact, higher interest could ultimately be bullish for oil and other commodities in the longer term as producers would be negatively impacted from the cost of borrowing.

WTI & ICE Brent Crude price movement

Source: Bloomberg

OPEC members crude production



Basket Price USD/bbl 48.63 as of 3/14 Quota MMbpd 30 Data Source Bloomberg Energy Intelligence Group

Production ('000 b/d)	Feb	Jan	Chg	Capacity
Total OPEC	32,165	32,230	-65	36,405
Algeria	1,040	1,040	0	1,150
Angola	1,690	1,670	+20	1,870
Ecuador	535	530	+5	555
Gabon	180	195	-15	220
Iran	3,830	3,800	+30	4,000
Iraq	4,440	4,490	-50	4,700
Kuwait	2,710	2,710	0	3,000
Libya	700	690	+10	780
Nigeria	1,680	1,640	+40	2,200
Qatar	620	615	+5	780
Saudi Arabia	9,780	9,870	-90	11,500
U.A.E.	2,950	2,950	0	3,150
Venezuela	2,010	2,030	-20	2,500

Source: Bloomberg

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