

Economic Analysis

Weekly Focus: Inflation and FOMC Minutes

Kim Chase

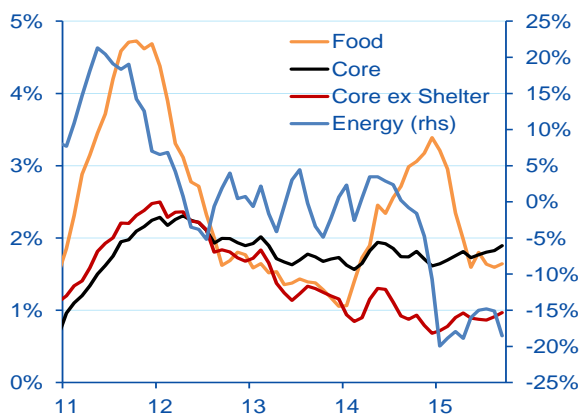
Headline Inflation Facing the End of the Energy Price Drag

Oil prices began their dramatic decline nearly fifteen months ago, and we are finally reaching the end of the road. Although oil prices are still low, levels are at the very least stabilizing. As a result, we should expect to see an impact on headline inflation in the coming months as the base effect for year-over-year growth works in our favor, pushing inflation back into positive territory. There has still been some downward pressure on natural gas prices, but stabilization in oil prices should prevent significant declines in headline inflation as we move into 2016. However, the continued declines in import and producer prices for October suggest a lingering drag from the slow global economy that may weigh on CPI for the month. We should also see a similar trend emerge for core commodities inflation, which has been stuck below zero since April 2013, though this may take a bit longer given the ongoing weakness in the global economy as a whole. For now, **October's CPI report (Tuesday)** should show the beginning of the end for negative headline inflation as well as further gains in core inflation inching closer to the Fed's target.

FOMC Minutes to Help Clarify Confidence in Inflation Reaching 2% Target

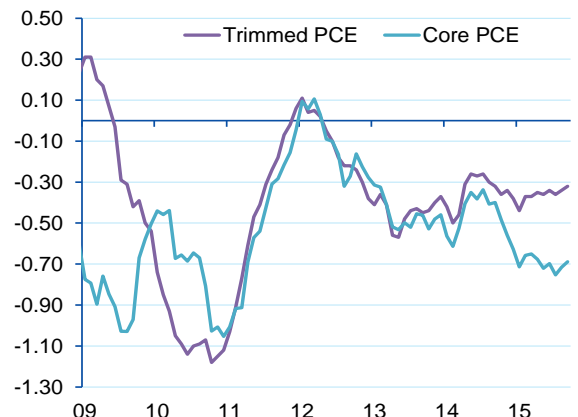
While CPI inflation is more relevant for markets, the FOMC tends to focus on PCE inflation in order to support their monetary policy strategy. The 2% inflation target applies to core PCE, not to CPI, and lately the two series have diverged more than normal. Core PCE has not yet recovered from the sharp drop back in 3Q14, though core CPI has almost fully rebounded. This is going to be an important trend to watch as we approach the December FOMC meeting – even though the signals for liftoff are stronger now than they were back in September, persistently low inflation remains a key concern. It will be interesting to see more details on the inflation-related discussion in the **October FOMC meeting minutes (Wednesday)**, and we expect that at least some members are still not “reasonably confident” that inflation will move back towards their target in the medium-term. If some of the dovish members decide to look at trimmed PCE inflation instead of core, the hawks may be able to muster up more support for a rate hike by the end of the year.

Graph 1
CPI Inflation (YoY % Change)



Source: BLS & BBVA Research

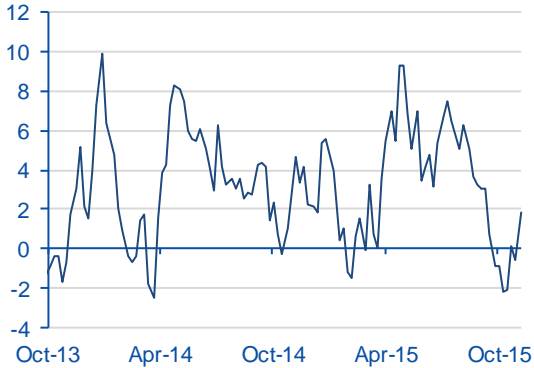
Graph 2
FOMC Target Gap: Inflation (Percentage Points)



Source: BEA, FRB, & BBVA Research

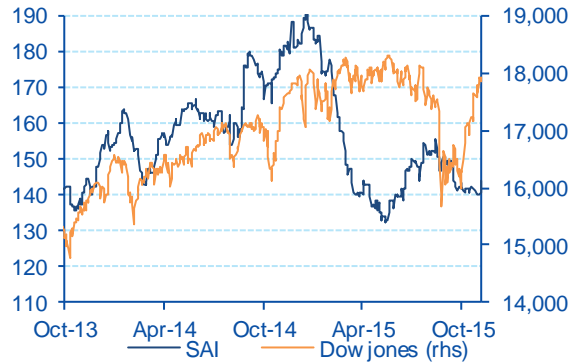
Economic Trends

Graph 3
BBVA USA Weekly Activity Index (3 month % change)



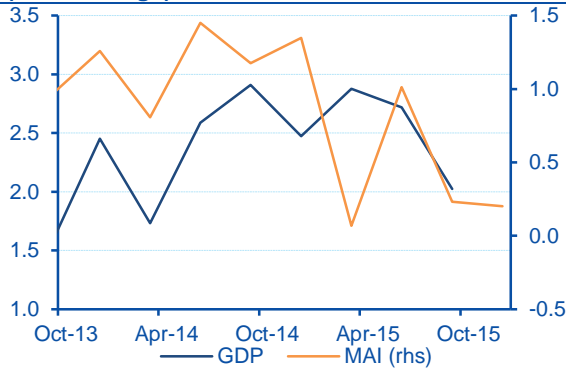
Source: BBVA Research

Graph 4
BBVA USA Surprise Activity Index & Dow Jones (Index 2009=100 & eop)



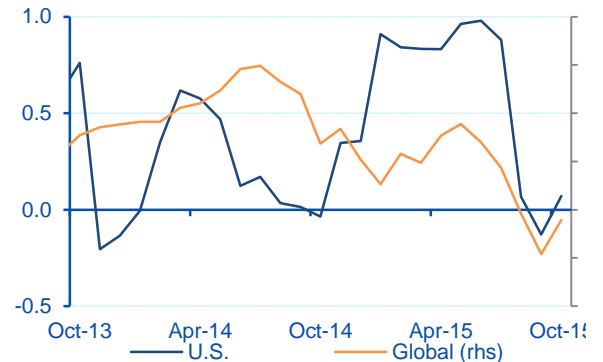
Source: Bloomberg & BBVA Research

Graph 5
BBVA USA Monthly Activity Index & Real GDP (4Q % change)



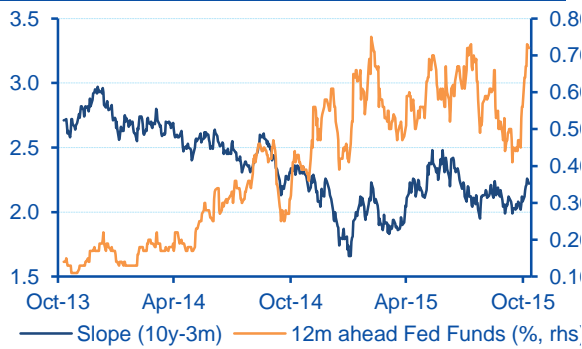
Source: BBVA Research & BEA

Graph 6
BBVA USA Risk Index (> 0 = increasing risk)



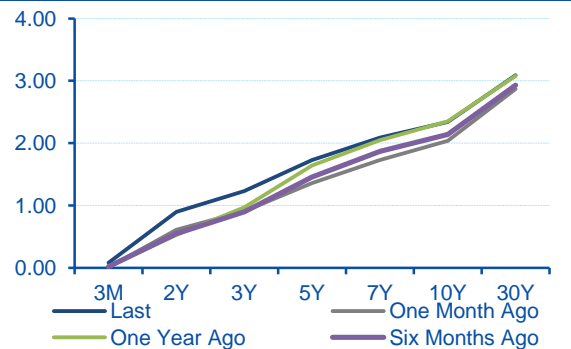
Source: BBVA Research

Graph 7
Fed Futures & Yield Curve Slope (% & 10year-3month)



Source: Haver Analytics & BBVA Research

Graph 8
U.S. Treasury Yield Curve (% p.a.)



Source: Haver Analytics & BBVA Research

Week Ahead Economic Calendar

Date	Event	Period	BBVA	Consensus	Previous
16-Nov	US Empire State Manufacturing Survey General Business Conditions SA	NOV	-10.10	-5.00	-11.36
17-Nov	US CPI Urban Consumers MoM SA	OCT	0.00	0.18	-0.20
17-Nov	US CPI Urban Consumers Less Food & Energy MoM SA	OCT	0.20	0.20	0.20
17-Nov	US Industrial Production MOM SA	OCT	-0.10	0.10	-0.19
17-Nov	US Capacity Utilization % of Total Capacity SA	OCT	77.40	77.50	77.54
17-Nov	US Industrial Production Industry Groups Manufacturing MoM SA	OCT	-0.10	0.00	-0.10
17-Nov	National Association of Home Builders Market Index SA	NOV	63.00	64.00	64.00
18-Nov	US New Privately Owned Housing Units Started by Structure Total SAAR	OCT	1190.00	1159.00	1206.00
18-Nov	Private Housing Units Started by Structure Total Monthly % Change SA	OCT	-1.33	-3.90	6.50
18-Nov	Private Housing Authorized by Bldg Permits by Type Total SAAR	OCT	1147.00	1140.00	1105.00
18-Nov	Private Total Housing Authorized by Building Permits MoM SA	OCT	3.80	3.17	-4.80
19-Nov	US Initial Jobless Claims SA	14-Nov	272.00	270.00	276.00
19-Nov	US Continuing Jobless Claims SA	7-Nov	2170.00	2155.00	2163.00
19-Nov	Conference Board US Leading Index MoM	OCT	0.20	0.50	-0.20
19-Nov	Philadelphia Fed Business Outlook Survey Diffusion Index General Conditions	NOV	-4.10	0.00	-4.50

Economic Outlook

	2015		2016		2014	2015	2016	2017
	2Q	3Q	4Q	1Q				
Real GDP (% SAAR)	3.9	1.5	3.1	1.9	2.4	2.5	2.5	2.4
CPI (YoY %)	0.0	0.1	0.9	2.2	1.6	0.2	1.8	1.9
CPI Core (YoY %)	1.8	1.8	1.9	1.9	1.7	1.8	1.8	1.9
Unemployment Rate (%)	5.4	5.2	5.0	5.0	6.2	5.3	4.9	4.6
Fed Target Rate (eop, %)	0.25	0.25	0.50	0.50	0.25	0.50	1.00	2.00
10Yr Treasury (eop, % Yield)	2.36	2.17	2.33	2.43	2.21	2.33	2.51	3.21
US Dollar/ Euro (eop)	1.12	1.12	1.07	1.08	1.23	1.07	1.13	1.16
Core Logic Home Prices (YoY %)	5.14	5.62	7.51	7.70	7.67	5.80	4.66	2.45

Fun Fact

The U.S. hot sauce market has grown by 150% since 2000, which is more than that of BBQ sauce, ketchup, mayonnaise, and mustard combined. (Euromonitor, October 2015)

Recent Publications

[State Monthly Activity Index: States Gathering Momentum into Fourth Quarter](#) (November 6, 2015)

[Strong Jobs Boost Probability for December Liftoff](#) (November 6, 2015)

[3Q15 Productivity Reflects Slowdown in Output and Hours Worked](#) (November 5, 2015)

[3Q15 GDP Growth Slows to 1.5% as Expected](#) (October 29, 2015)

[FOMC Statement: Rate Remains Unchanged as FOMC Hopes for December Liftoff](#) (October 28, 2015)

[U.S. Real GDP Growth Nowcast: 1.49% for 3Q15](#) (October 26, 2015)

[CRE Going Strong, at Least for the Time Being](#) (October 26, 2015)

[U.S. Auto Industry Chartbook 3Q15](#) (October 26, 2015)

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