

FOMC preview

QE programme in focus

- **Focus is on asset purchases and, with a review of the QE programme scheduled for this meeting, we are likely to get new information.**
- **We do not expect changes to the current pace of purchase or to the forward guidance on interest rates.**
- **The FOMC could choose to include individual forecasts for the Fed's balance sheet in the economic projections and signal that assets could be held to maturity.**
- **We expect the tone at the press conference to be balanced but markets are sensitive to changes in the QE language and there is room for higher US rates.**

QE review – will it bring any changes?

The March FOMC meeting is set to contain a lot of information. On top of the statement, we expect to receive updated economic projections and Bernanke's comments at the press conference. While we do not expect the statement to alter the pace of asset purchases from the current USD85bn per month or change the forward guidance on interest rates, the meeting is nevertheless interesting.

In particular, the minutes from the January FOMC meeting stated that a review of the asset purchase programme was on the agenda for the March meeting. At least three questions are likely to be discussed. First, we expect a review of the potential costs versus benefits of expanding the balance sheet further. Second, what will decide when the Fed should end its purchases? Third, should the Fed change the June 2011 exit strategy and keep its assets on the balance sheet to maturity.

Given the relatively dovish comments from Bernanke and Yellen in recent speeches, we expect the language on the QE programme to reflect that a majority in the FOMC still see the benefits of more QE exceeding the potential costs. Although the Fed would like to be clear in its communication, we the language in the January statement saying that QE will continue until it sees a 'substantial improvement' in the labour market will probably have to suffice. One way to improve the guidance, however, would be to add individual participants' forecasts of the expected path of the balance sheet in the Summary of Economic Projections. We see a likelihood of such a move tomorrow.

In terms of the exit strategy and in particular when the Fed will start selling its assets, we are likely to have to wait until the minutes are released to get full information. Bernanke is likely to get the question at the press conference and he is likely to signal that the Fed could choose to keep its assets to maturity. The big question is whether holding the assets longer would mean lower purchases today. If Bernanke signals that the Fed is considering such a substitution it would be likely to be interpreted as hawkish and send US rates higher.

FOMC meeting 19-20 March

- 19:00 FOMC statement
- 19:00 Economic projections
- 19:30 Bernanke holds press conference

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Economic progress is likely to get mentioned

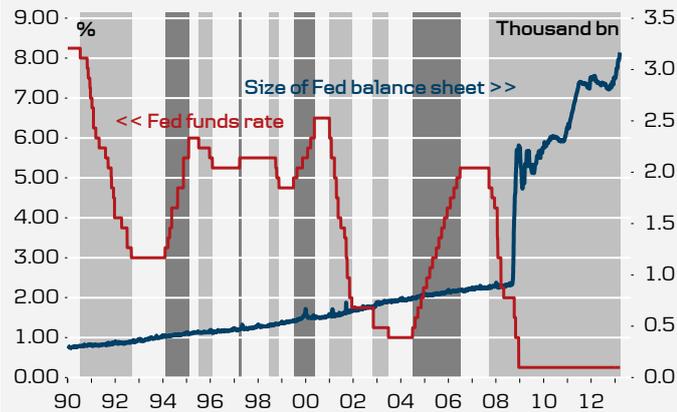
The FOMC statement is likely to note the past months' stronger-than-expected data and the improvement in labour market indicators. We do not expect this to show in the economic projections though, as they were already upbeat in December with expected growth in 2013 at 2.7% Q4/Q4 (Danske Bank expects 2.4% Q4/Q4). In terms of inflation, we expect the language to be in line with the January statement.

Room for higher US rates

With the discussion of 'the cost and risk arising from asset purchases in the January minutes, we saw how sensitive the market is to potential changes in the QE programme. The market clearly interpreted the statements as hawkish; equities sold off, the USD got bid against most other currencies and 10Y US Treasuries sold off. Although we expect the tone from the press conference to be very balanced, there is no doubt in our minds that the market will scrutinise every wording and we see risks skewed towards negative surprises and sell offs. Yields on 10Y Treasuries are now in the middle of the past trading range and, from a technical point of view, there is room for an increase following the meeting.

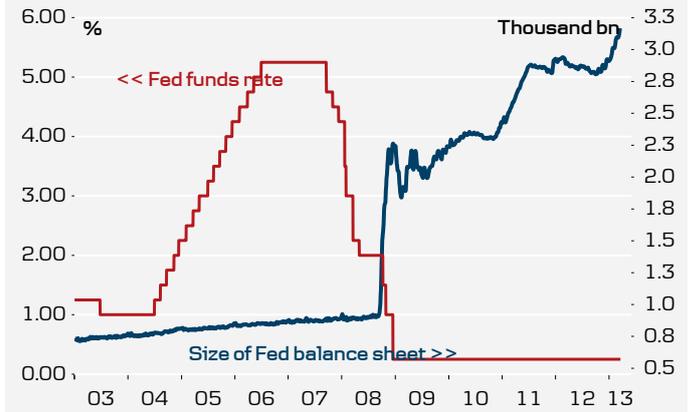
See the charts on the following pages.

Balance sheet expansion has shifted to a higher gear



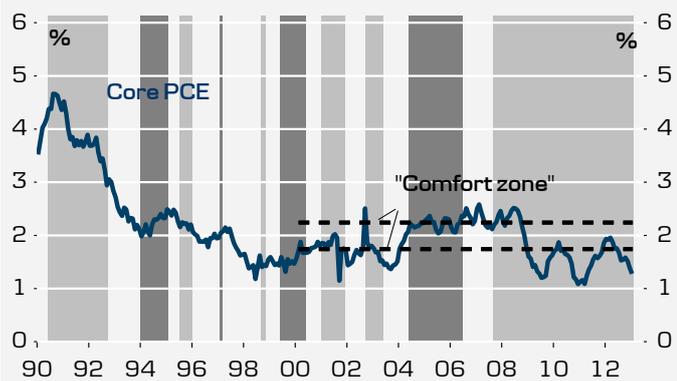
Note: Dark (light) shading indicates periods of tightening (easing)
Source: Reuters EcoWin, Danske Bank

Currently, the Fed is buying assets of USD85bn per month



Source: Reuters EcoWin

Core PCE inflation below Fed's comfort zone...



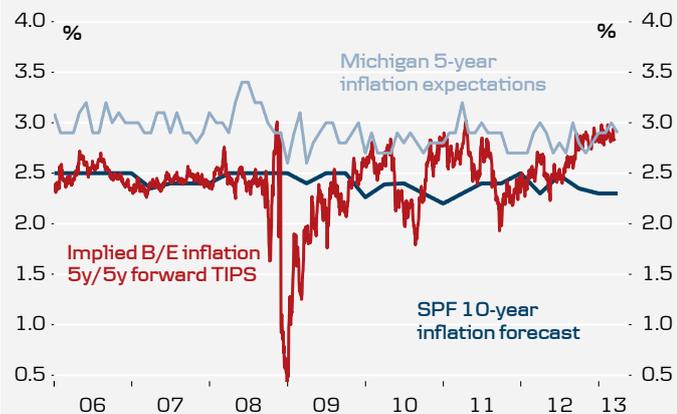
Note: Dark (light) shading indicates periods of tightening (easing)
Source: Reuters EcoWin, Danske Bank

...and inflation risks are balanced



Source: Reuters EcoWin, Danske Bank

Break-even inflation has moved higher following QE3



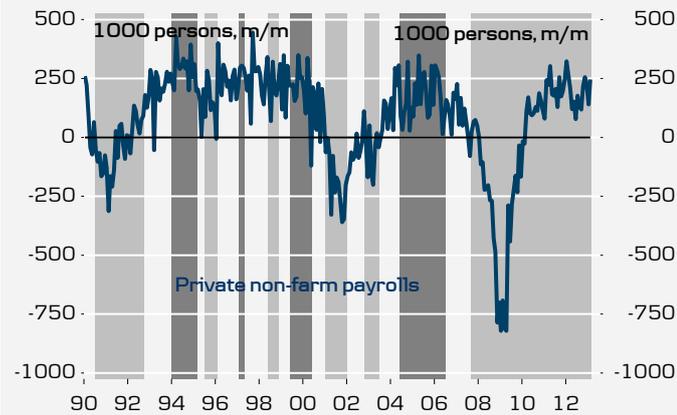
Source: Reuters EcoWin, Danske Bank

ISM indexes in line with other strong data over past months



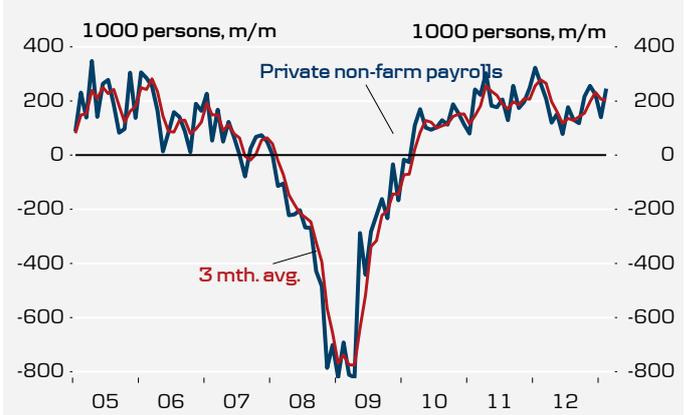
Source: Reuters EcoWin, Danske Bank

Job growth remains moderate...



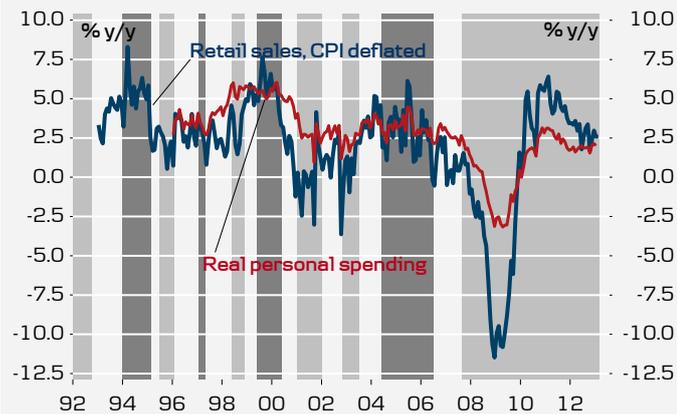
Note: Dark (light) shading indicates periods of tightening (easing)
Source: Reuters EcoWin, Danske Bank

...but the trend has improved



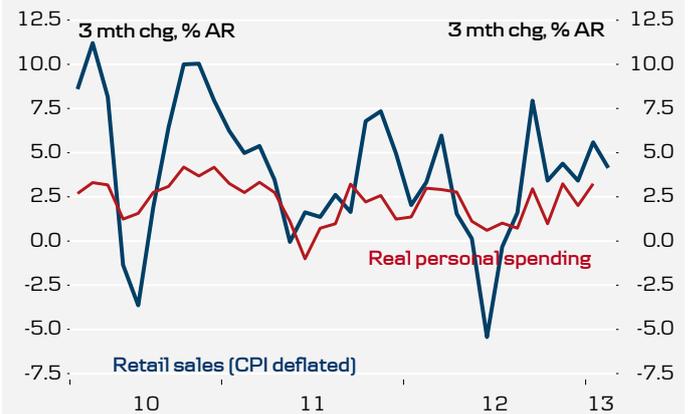
Source: Reuters EcoWin, Danske Bank

Consumer spending has been okay...



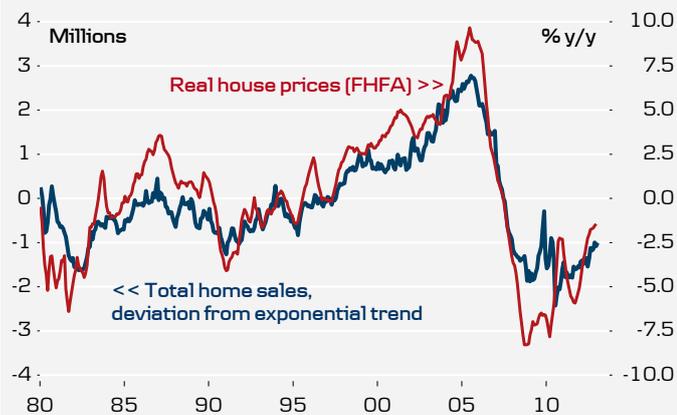
Note: Dark (light) shading indicates periods of tightening (easing)
Source: Reuters EcoWin, Danske Bank

...but will be hit by a tax hike this year



Source: Reuters EcoWin, Danske Bank

Housing market data has shown improvement



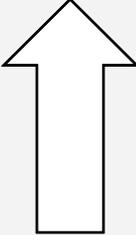
Source: Reuters EcoWin, Danske Bank

Interest rates at very low levels



Source: Reuters EcoWin, Danske Bank

FOMC ornithology

	2012	2013	2014	
 <p>HAWKISH</p>	Fisher	Fisher	Fisher	<i>Dallas</i>
	Plosser	Plosser	Plosser	<i>Philade</i>
	Lacker	Lacker	Lacker	<i>Richmc</i>
	George	George	George	<i>Kansas</i>
	Lockhart	Lockhart	Lockhart	<i>Atlantc</i>
	Bullard	Bullard	Bullard	<i>St. Lou.</i>
<p>NEUTRAL</p>	Duke (B)	Duke (B)	Duke (B)	<i>Board</i>
	Powell (B)	Powell (B)	Powell (B)	<i>Board</i>
	Pianalto	Pianalto	Pianalto	<i>Clevela</i>
	Bernanke (B)	Bernanke (B)	Bernanke (B)	<i>Chairm.</i>
	Tarullo (B)	Tarullo (B)	Tarullo (B)	<i>Board</i>
	Raskin (B)	Raskin (B)	Raskin (B)	<i>Board</i>
 <p>DOVISH</p>	Stein(B)	Stein(B)	Stein(B)	<i>Board</i>
	Kocherlakota	Kocherlakota	Kocherlakota	<i>Minne</i>
	Williams	Williams	Williams	<i>San Fa</i>
	Dudley	Dudley	Dudley	<i>New Yc</i>
	Yellen (B)	Yellen (B)	Yellen (B)	<i>Board</i>
	Evans	Evans	Evans	<i>Chicag</i>
Rosengren	Rosengren	Rosengren	<i>Boston</i>	

Bold signifies voting right (B) signifies board member

Source: FOMC, Danske Bank Markets

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